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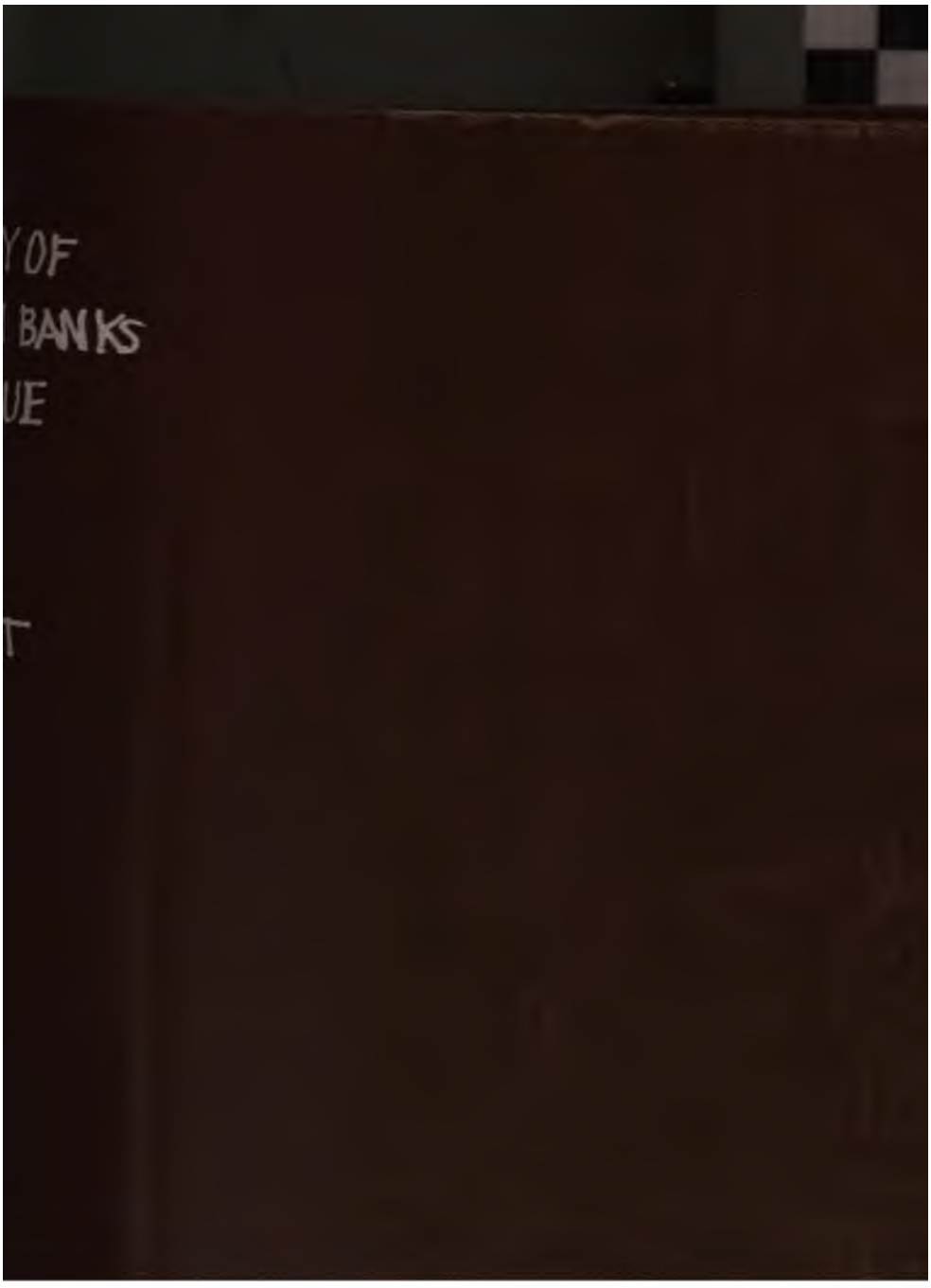
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A HISTORY OF MODERN BANKS OF ISSUE

WITH AN ACCOUNT OF THE ECONOMIC CRISES OF THE PRESENT CENTURY

BY

CHARLES A. CONANT

G. P. PUTNAM'S SONS

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To

MY MOTHER

PREFACE.

THE reason for being of this work is the growing interest in the United States in financial and economic subjects and the fact that they promise to be the paramount issues of American politics for many years to come. My purpose has been to bring together, in compact form, the leading facts regarding the banks of the world authorized to issue circulating notes and the history of the financial and economic crises through which they have passed. There is no work in English covering exactly the ground covered by the *History of Modern Banks of Issue*. The materials for such a history are accessible in public records as well as special works, but they have never before been brought together in a form easily accessible to the American and English reading public.

The functions and character of history have changed with the changes in the character of national development. The historical development of the human race has passed through two essential stages and has entered upon a third. The first was the struggle for the existence of civilization and national life; the second was the struggle for the legal and political freedom of the individual within the state; the third is the struggle for the complete development, according to sound economic laws, of the producing capacity of the community. The Muse of History has followed no unreasoning whim in turning her pen to the story of each successive stage of the world's progress. In the first stage of her work, her theme was the history of nations and the acts of their sovereign powers. In the second stage, the history of

value to the community became the history of the people and the contest for popular rights. The historians of each age have been logical in looking to the dominant spirit of that age.

The issue of the present and of the immediate future,—and the subject with which the Historic Muse must most concern herself,—is the best means of developing the possibilities of individual and national life. This issue is essentially an economic one and the history of economic development must, in the very nature of events, be in future the principal study of practical thinkers and workers. The Massachusetts Senator who declared that of late years the American people had given "too much attention, perhaps, to economic questions, and too little attention to those great and far-reaching questions on which the future of the republic depends,"[1] spoke out of the education and out of the political theories of the past and with his face to the past rather than to the future. The pursuit of the best means of increasing wealth, not for its own sake, but for the wider opportunities of intellectual and moral development which it places in the hands of the community, is the mission of the student of public affairs for the future, and the public man who seeks different political ends subjects himself to the judgment pronounced upon himself by Lord Stanley a generation ago, that he was brought up in the pre-scientific period.[2]

Political economy is still in a large measure an experimental and a disputed field, but this is less true of financial administration than of the questions of taxation and the distribution of wealth, which still perplex economic students. The modern banking community have already learned, during the past hundred years of the history of banking, the leading lessons of the failures and experiments of that period. There is doubtless much yet to be learned, but the system of a banking currency and of the management of banking operations is now a practicable and workable system. The

[1] Congressional Record, Fifty-third Congress, Third Session, March 2, 1895, p. 3108.

[2] McCarthy, I., 31.

results of the experiments of the century can be summed up and their lessons indicated in a clear and certain manner, subject to little dispute by those who have given unprejudiced study to the subject. It is these experiments which I have endeavored to describe in the following chapters, leaving their lessons for the most part to be derived from a comparison of their results with the rules of sound banking policy.

The purpose of this work is historical rather than controversial and I have even refrained from discussing the problem of the single or double standard, because the rules which govern a banking currency apply with equal force, whatever metal constitutes the standard money of redemption. I have thought it proper to state, as simply and as clearly as possible, the theory of a banking currency, but I have endeavored to avoid all digressions which were not essential to an understanding of the history of banks of issue and of recent events in the financial world. Systems of coinage, the history of public loans and political events, the many forms of mortgage, deposit and popular banks, and the new problems relating to the uses of speculation and the part played by negotiable securities in modern economic life, are such important subjects of discussion that each is worthy of separate treatment, and they are only referred to here where they seem to form a necessary part of the history of one of the great banks of the world. It has been necessary to refer in several cases to the history of government paper money, because it is related to the origin and growth of banks of issue, but my plan excludes the systematic treatment of paper money, which would of itself fill a volume. My chief object, beyond that of a narrator, will be accomplished if the study of the dismal record of government interference with monetary laws shall convince thinking Americans of the axiomatic truth that—

The currency of a commercial country should be regulated by commercial conditions and not by the whims of politicians.

CHARLES A. CONANT.

WASHINGTON, D. C., *April* 1, 1896.

I beg to acknowledge my obligations to the Hon. William E. Curtis, Assistant Secretary of the Treasury; to the Hon. James H. Eckels, the Comptroller of the Currency; and to the Hon. Robert E. Preston, the Director of the Mint, for the use of many valuable public documents of foreign countries as well as of the United States; to them, and many other officers of the Treasury, to the Hon. Lewis Sperry of Hartford, Conn., and to Mr. L. Carroll Root of New York, for many helpful suggestions; and to my Secretary, Miss Florence Johnson, for her intelligent assistance.

Amounts expressed in foreign currency in the following pages are reduced only to round sums in United States money, with sufficient frequency to afford a general idea of the sums dealt with, but the exact equivalent of the foreign monetary unit is usually stated early in the chapter in which it appears.

The full titles of the leading authorities cited will be found at the back of the book.

C. A. C.

CONTENTS.

CHAPTER I.

PAGE

THE THEORY OF A BANKING CURRENCY 1

CHAPTER II.

ANCIENT AND MODERN BANKING IN ITALY 21

CHAPTER III.

BANKING IN FRANCE 38

CHAPTER IV.

FIRST CENTURY OF THE BANK OF ENGLAND 78

CHAPTER V.

SECOND CENTURY OF THE BANK OF ENGLAND 100

CHAPTER VI.

THE SCOTCH BANKING SYSTEM 138

CHAPTER VII.

BANKING IN IRELAND 167

CHAPTER VIII.

THE BANKS OF GERMANY 182

CHAPTER IX.

PAGE

THE AUSTRO-HUNGARIAN BANK 209

CHAPTER X.

THE BANK OF RUSSIA 235

CHAPTER XI.

THE BANKS OF NORTHERN EUROPE 250

CHAPTER XII.

THE BANKS OF SOUTHERN EUROPE 268

CHAPTER XIII.

THE BANK OF THE UNITED STATES 286

CHAPTER XIV.

THE STATE BANKING SYSTEMS 310

CHAPTER XV.

THE NATIONAL BANKING SYSTEM 348

CHAPTER XVI.

THE CANADIAN BANKING SYSTEM 386

CHAPTER XVII.

THE BANKS OF LATIN AMERICA 413

CHAPTER XVIII.

BANKING IN AFRICA AND THE EAST 432

CHAPTER XIX.

CRISES AND THEIR CAUSES 453

CHAPTER XX.

PAGE
THE EARLY CRISES OF THE CENTURY 467

CHAPTER XXI.

THE LATER CRISES OF THE CENTURY 492

CHAPTER XXII.

THE CRISIS OF 1893 524

CHAPTER XXIII.

THE ADVANTAGES OF A BANKING CURRENCY 554

LIST OF AUTHORITIES 577

HISTORY OF MODERN BANKS OF ISSUE.

CHAPTER I.

THE THEORY OF A BANKING CURRENCY.

The Distinction between Bank-notes and Money—The Functions of Currency as a Standard of Value and Medium of Exchange—The Mechanism of a Bank of Issue—Do Note Issues Create Capital?—Importance of Redemption in Coin on Demand—The Necessity for Quick Assets—The Operation of the Rate of Interest and the Foreign Exchanges on the Volume of Circulation—Difficulty of "Cornering" Money under Free Banking.

IT is the purpose of this work to give the outlines of the history of the leading banks of issue in the world and their methods of doing business, and incidentally to set forth the principles and uses of a banking currency. Banking can be done without the issue of bank-notes, but they are an important factor in the devolopment of the use of capital and afford the best currency for general uses. In their capacity as a circulating medium, bank-notes have come to be confused with money and have attained in the minds of many a special and official character different from that of other commercial paper. The examination of the history of banks of issue, as well as of the theory of a banking currency, will serve to show the gradual development of the use of bank-notes as a means of transferring credit and the part they play in commercial transactions alongside of other

forms of credit which differ from them only in degree of negotiability.

The creation and regulation of a banking currency are based upon the theory that bank-notes are a convenient means of giving mobility to capital. There are two important truths which should be clearly understood at the outset of the discussion of banking and paper currency. They are:

1. That bank-notes are not money.

2. That bank-notes are a form of credit and are of substantially the same nature as bills of exchange, promissory notes, and checks.

The distinction between bank-notes and money is of prime importance for the purposes of economic study and from the standpoint of legislation, if not always important in daily transactions. It will be convenient, however, first to point out what bank-notes are, before considering what they are not. It will be convenient also to state broadly, in the beginning, the theory of a banking currency and of free banking, as a theory, before dealing with certain limitations, for the purpose of promoting uniformity and security, which experience and sound judgment may suggest in practice.

Bank-notes are the proper instruments of commercial transactions because they are the creatures of commercial needs and are adapted in volume and use to commercial necessities. In this respect they differ from government paper money, which is regulated wholly by the necessities of governments and not by the convenience of trade. Bank-notes are substantially similar to checks and bills of exchange, because they are simply the paper representatives of credit. In the language of Prof. Bonamy Price:

> A seller by taking the bank-note makes himself the creditor of the government or bank, and is willing to part with his property, substantially, on credit to the state or bank. He finds in this debt, now due to him, of the issuer of the bank-note a sufficient guarantee for being able to buy with it other goods. . . . Every buyer with a note virtually says, "I have no money; give me the goods and I will tell a good man who owes me money to pay you for me." [1]

[1] *Currency and Banking*, 42–43. The character of a bank-note is clearly and simply defined by Prof. Charles F. Dunbar, professor of

Those who insist that gold and silver constitute the only proper medium of financial transactions do not clearly distinguish the two essential functions of currency. These functions are the creation of a standard of value and the provision of a means of exchange. It is only in the fulfilment of the first function that exchange value is required in the material of which the currency is made. The fulfilment of the second function requires only that the currency shall represent value, rather than that it shall contain value in itself.[1] A bank-note currency represents the value bound up in commodities which are in process of production and exchange. The essential function of business operations is the production and exchange of commodities for each other,—not the exchange of barren heaps of metal for each other nor of commodities for metal. The intervention of gold and silver in such exchanges adds nothing to the sum of production and is not necessary to carry them on, except as the metals afford, with paper, a convenient tool of exchange

---

political economy in Harvard University, as follows: "The bank-note is the duly certified promise of the bank to pay on demand, adapted for circulation as a convenient substitute for the money which it promises. It is issued by the bank, and can be issued only to such persons as are willing to receive the engagement of the bank in this form instead of receiving money, or instead of being credited with a deposit."—*Theory and History of Banking*, 16.

[1] It is difficult to get away from the term "intrinsic value," in the terms of ordinary discussion, in spite of the well-reasoned demonstration of Prof. MacLeod that value is a relation based upon exchange rather than an inherent quality.—*Elements of Banking*, 12. Gold and silver, strictly speaking, are not only limited to an exchange value, but they perform to a large extent, by the convention of civilized nations, the same functions in monetary uses, as representatives of value, as bank-notes and other commercial instruments. Roscher illustrates the fact that even the currency of gold as money rests in a measure upon credit. "The person who takes money as such must always harbor the hope of being able to dispose of it again as money. . . . The savage Goahiros, between Rio de la Hacha and Maracaibo, are too 'distrustful' to take anything in trade but commodities fit for the most immediate use."—*Political Economy*, I., 351. The refinement in the use of credit is a pretty accurate measure of national economic progress.

and, by themselves, a standard and common denominator by which exchanges are measured. Bank-notes are not, as government paper money usually is, pieces of paper created out of nothing to represent value. They are simply the paper representatives of a great mass of mercantile transactions. They are the convenient counters by which men carry on exchanges. The presence of gold and silver is a necessary element in these exchanges only for the purpose of applying the test of a common and fixed standard, and this is secured for bank-notes by the condition that they shall be redeemable in standard coin on demand.

The entire fabric of a bank of issue constitutes a harmonious whole. The capital subscribed by the stock-holders at once becomes a liability and provides the bank with cash for making loans and keeping a coin reserve. The issue of notes enables the bank to furnish accommodation to the holders of good commercial paper by covering the paper into its assets and treating the notes as demand liabilities. A bank of issue, therefore, has on one side its liability to its stock-holders for their invested capital and its liability to its note-holders to pay coin on demand. It has on the other side, as its resources, the cash derived from subscriptions to the capital and the commercial paper payable in cash by its makers at maturity. When deposits are received in cash or paper convertible into cash, the proceeds can be employed to enlarge the scope of the discounts. The obligation to pay the deposit becomes a liability, but the cash deposited furnishes assets of equal volume as an offset. Most of the great banking institutions of the world have begun business, and many of them continue it to-day, upon their capital and their loans and with but a small proportion of cash deposits.

The volume of notes which a bank may issue, when not directly limited by law, is determined by a prudent relation between the issues and the coin reserve. The greater part of the cash received in capital and deposits, over and above the coin reserve, is available for loans and discounts. Loans as distinguished from discounts are actual advances of money

upon negotiable securities. They usually constitute a smaller proportion of the transactions of a bank in a commercial city than the commercial discounts. These are simply purchases by the bank of commercial paper, carrying the right to collect money at some future time. The wholesale merchant, for instance, receives from his retail customer a promissory note or bill of exchange, covering the cost of goods he has sold, payable sixty or ninety days from date. By taking this note or bill to the bank the wholesaler obtains currency at once for the amount contracted to be paid, less an interest charge which is known as discount. The business of a bank of issue is simply to transform the bill of exchange, which is itself a negotiable security, into another sort of negotiable security. For this purpose it issues bank-notes. In the concise language of an eminent French financial writer:

> The bank bill is a promise to pay a fixed sum at sight or to bearer. In promising to pay at sight, the difficulty is avoided of maturity at a fixed term and the bearer is relieved of the limitations which result from it. By the promise to pay to bearer, one gets rid of the embarrassment of endorsements, protests, recourse, etc. One obtains by this means a security always negotiable, to which suffices a signature generally known and in some degree public to make it equally accepted and demanded, even in preference to metallic money.[1]

The bank by the issue of notes gives mobility to capital in several ways. It enables the holder of a bill of exchange to put it to active use instead of locking it up against the time of its maturity. The wholesaler or manufacturer, by paying a small commission to the bank upon such a bill, is able to obtain in advance the use of capital in negotiable form to which he would otherwise not become entitled for several months. He is enabled to obtain it not only in advance of the time it would otherwise be due, but in such form that he can split it into small amounts and pay a part for his raw materials, a part for his labor, and a part for his personal expenditures. The issue of bank-notes also enables small depositors to combine their capital in the hands of the bank,

[1] Courcelle-Seneuil, 102.

so that it becomes available for constant use. This is one of the great advantages of modern banking, that it brings out into the light and into the current of the processes of production the capital which would otherwise be locked up in idle hoards. The bank-note is a loan from the holder, but a loan which costs him nothing and, on the contrary, affords him the benefit of security, convenience, and negotiability for his capital. In the sense in which government paper money, made by law a legal tender for the payment of debt, is a forced loan, for non-commercial uses, upon the productive forces of the community, the bank-note, which is not forced legal tender, is a voluntary loan, for commercial uses, which tends to bring into play, for the mutual benefit of borrowers and lenders, the full efficiency of those productive forces. [1]

The simple statement of the theory of a banking currency shows how absurd it is to imprison the volume of circulating notes within fixed limits, or to condition their issue, when they are kept in circulation at par with coin, upon any other specific thing than the amount of loanable capital. The Bank of England is limited in its note issues, beyond a fixed amount, by the Bank Act of 1844, to deposits of gold coin or bullion, with the result that there is an annual autumnal stringency in the money market.[2] There have been repeated periods of business paralysis when every possible substitute has been employed to make up for the deficiency of circulating notes, and the limitation itself has been finally suspended in every acute crisis as the only means of averting universal bankruptcy. The banks of issue of the United States are required to purchase evidences of the national debt and are allowed in circulation only ninety per cent. of

[1] Exactly the opposite view was urged by some of the early opponents of the Bank of England. Davenant declared that the effort to attract deposits by the offer of four per-cent. interest was a hindrance to energy and enterprise. Rogers, 18. This view overlooked the fact that the money would be loaned by the bank for active use.

[2] V. Jevons, *Investigations in Currency and Finance*, Ch. v., 160–93, —"The Frequent Autumnal Pressure in the Money Market."

the face value of these securities, with the result that as the debt has been reduced, the bank-note circulation has declined. The securities have reached an enormous premium as they have become scarce, and the bank-note circulation has fallen from $354,408,008 on June 30, 1875, to $211,600,698 on June 30, 1895, while loans and discounts, which indicate the volume of business, have more than doubled. The public, under these circumstances, have looked to other sources than the banks for a circulating medium and found it, until the repeal of the purchasing clause of the Sherman law, in purchases of silver bullion, by the Treasury, and the issue of government paper money in payment for the bullion. This circulation proved absolutely irresponsive to the demands of business and resulted, after periods of great stringency in the autumn of 1890 and the summer of 1893, in a long period of redundancy and gold exports during 1894 and 1895. The experience of both England and the United States in this respect justifies the judgment of those who believe that the circulating medium should be based upon the general assets of the banks and governed by business conditions rather than based upon extraneous securities and governed by their fluctuations in quantity or value.

The theory of a banking currency, as here defined, is in accordance with the "banking principle," which is approved by most bankers and writers upon political economy. There is another theory of bank-note issues, described in England under the name of "the currency principle," upon which the law governing the circulation of the Bank of England is based. The essential difference between the two theories is, that "the banking principle" regards bank-notes as similar to other commercial paper and their volume as properly subject to business requirements, while "the currency principle" regards bank-notes as performing the functions and possessing substantially the character of actual money and their volume as properly subject to regulations which will cause it to change in the same manner as a circulation entirely of coin. The failure of this principle to operate as expected by its supporters in the case of the Bank of Eng-

land will be set forth in the chapter relating to the later history of that bank. The theory is not applicable where credit exists in any form, and its advocates have never succeeded in advancing any substantial reason for assimilating bank-notes to coined money, except the fact that they enter, like money, into general circulation. This fact justifies certain regulations to secure uniformity and safety, but the regulations should be the same in kind as those which govern other commercial paper and evidences of indebtedness.

There is no reason why the number of bank-notes should be limited any more than other commercial paper, except by the requirement of redemption in coin on demand which serves as a test of their value and the solvency of their issuers. A bank authorized to issue circulating notes occupies, substantially, the position of a corporation or business firm,—the circulation of its notes depends upon its reputation for solvency and honesty. Government regulations requiring a mutual guarantee or the formation of a common safety fund may enable the notes to pass from hand to hand without inspection as to the particular institution putting them in circulation, but, even in such a case, the validity of the notes depends upon the solvency and resources of the united body of issuers, if not upon that of the individual issuer.

Prof. H. Dunning MacLeod, an acute and brilliant writer upon the laws of banking, undertakes to show that the issue of instruments of credit is in itself the creation of capital. He brings many arguments to the support of his position, but his strongest argument is a legal rather than an economic one. He shows plainly enough that there is an essential distinction in law between the personal deposit (*depositum*) secured by a warehouse receipt, entitling the holder to the return of the specific goods deposited, and the creation of a debt (*mutuum*), by which the lender is simply entitled to the return of some equivalent, but not the specific thing entrusted to the borrower. The claim in the first case is specific, and possession of the article may be recovered by a writ of replevin, but it constitutes in the other case only

a general claim against the entire assets of the borrower. Professor MacLeod is doubtless right, as a proposition of mathematics or of law, in his demonstration that the new obligations created by evidences of debt are not properly set off against specific property in the hands of the debtor. The holder of a bank-note for ten dollars has no claim against any specific ten dollars in the cash drawer of the bank ; he simply has a legal claim for an equivalent for the amount.[1]

But Professor MacLeod, in his subtle argument upon this subject, confuses the domains of law and mathematics with the domain of economics. Political economy looks deeper than legal distinctions and looks to the substance behind algebraic formulæ. The creation of paper credit from this point of view is not an addition to existing capital. It greatly assists in the movement of capital and, in individual cases, the creator of paper credit may obtain the use of more capital than he possesses, but in every such case he simply obtains the use of the capital of some other person or body of persons. Barring the question of the incorporeal wealth arising from mental culture, economics deal with tangible property. Negotiable securities represent tangible property, either in the possession of the issuers or in the possession of the holders of the securities who are willing to advance their capital for the promotion of some enterprise. The individual who borrows beyond the limits of his tangible capital simply obtains the use of some other person's capital. In the words of Professor Émile de Laveleye :

[1] The legal distinction is important enough to a correct comprehension of the laws of banking to justify giving it in Prof. MacLeod's own words : "The essential feature of a 'Banker' is, that when his customers pay in money to their accounts, *they cede the property in the money to the Banker.* The money placed with him is not a Depositum, or Bailment ; but it is a *Mutuum :* it is a Loan, or Sale, directly to himself. The 'Banker' buys the money from his customer ; and in exchange for it, he gives his customer a Credit, or Right of action to demand back an equivalent amount of money at any time he pleases ; which Right of action he is also at liberty to transfer to any one else he pleases."—*Theory and Practice of Banking*, I., 319.

> Credit seems to multiply capital because by the side of the thing due appears the promise which gives a right to its possession; but in fact there are not two things,—one is only the shadow of the other. Burn every evidence of credit; nothing real would cease to exist. Juridicial relations only are changed. The creditors lose exactly what the debtors gain.[1]

A bank of issue, therefore, creates no new capital when it issues its notes to the amount of its assets available beyond its coin reserve. It simply takes the titles to capital which have been transferred to its custody and loans them to its customers in the form of negotiable paper. This paper, under a system of free banking, differs in no respect, except its greater degree of transferability, from personal promissory notes and bills of exchange. The bank, whether by its intrinsic reputation or by the requirements of certain uniform laws, simply affords a definite and well-known security and a uniform style of note paper which add to the convenience of the business community.

Banking can be done without the issue of circulating notes, and is done to a large extent in the greatest commercial centres, simply by the use of checks. Checks came into extensive use in England as a means of transferring credit when the Bank of England was given by law the substantial monopoly of the issue of circulating notes. The use of checks or other instruments of credit than bank-notes usually obtains the widest development where the modern commercial system of credit and of business has attained it highest form. As Professor Dunbar forcibly says of this medium of exchange:

---

[1] *Éléments d'Économie Politique*, 221. If Prof. MacLeod's theory is correct, the estimates of aggregate national wealth should be obtained by adding to the ascertained value of corporate property the face or market value of the securities which represent it, and in this way the country in which "stock watering" prevailed to the greatest extent would be that possessing the most wealth. Prof. MacLeod himself says, "that a nation can *spend* its money in destroying its enemies and *have* it too as bank-notes, or currency, is a wild and mischievous delusion."—*Theory and Practice of Banking*, II., 267.

Of the entire circulating medium of this country it forms incomparably the greatest, although the least considered, part. Depending for its efficiency solely upon convention and issued as well by private firms as by incorporated banks, it for the most part eludes the regulations which legislatures so industriously enforce upon the other constituents of the currency. Indeed, beyond the requirement of a minimum reserve to be held by incorporated banks, made by the law of the United States, we may say that the subject is not touched by legislation, in this country or elsewhere. The necessity for payment in specie upon demand, which is the most important safeguard of value, is the result of the general provision for the payment of debts of any kind.[1]

The essential question for every one who believes in developing the productive powers of the community to their utmost limit is the best method of giving mobility to capital in that community. Checks and book credits are valuable and essential instruments of modern commerce, but they cannot always be so readily introduced into general use as bank-notes may be. The difference is wholly one of the business habits of a community, of its business necessities and of the development of banking. The governing principle of banking is that mobility should be given to capital by the best means which will be accepted by the community. Bank-notes afford this means in new countries and those in which banking is undeveloped.

There is no more risk in the issue of bank-notes within fixed legal proportions to capital or assets, when they are redeemable in coin on demand, than in drawing checks or bills of exchange. There is no more danger of the inflation of values or of the volume of money, for the two transactions are essentially the same. The question of the solvency or soundness of the bank and its paper issues is in both cases chiefly one of good banking. Inflation by bank-note issues, when banks are required by law and by commercial custom to redeem their notes in coin on demand, is not conceivable in any such sense as inflation by means of government paper money, issued without regard to the demands of business and incapable of contraction with the diminution of those demands.

[1] *Theory and History of Banking*, 44–45.

The inflation of paper credit is one of the evils of the structure of modern industry and banking which forms a drawback to its manifold benefits, but bank-notes as such have never played more than a subsidiary part in such inflation. The evil arises from the abuse of credit, from the sinking of capital in unproductive enterprises, from speculative risks, and from over-sanguine calculations which sometimes result in unsound banking. But unsound banking is not especially connected with the issue of bank-notes and has occurred again and again with banks of mere discount and deposit and with banks like that of Hamburg, which held coin to the full value of their circulating notes. The crisis of 1893 in the United States is the most recent illustration that such incidents are rarely due to the abuse of bank-note issues. The bank-note currency was then restricted to the trifling proportion of about one-eighth of the entire monetary circulation of the country and was less than for many years before. Nearly every decade of the past century has witnessed a commercial crisis, but in no case could it be traced to the over-issue of bank-notes convertible into coin on demand. The speculative mania has ebbed and flowed, but bank-notes have not been the cause of either ebb or flood unless where coin redemption was suspended in fact or by the intervention of law. So complete is the evidence that bank-note issues have not been an essential factor in causing fluctuations in prices and collapses of credit that Mr. Tooke, the eminent English economic student, after painstaking investigation declared:

> In point of fact and historically, as far as my researches have gone, in every signal instance of a rise or fall in prices, the rise or fall has preceded, and therefore could not be the effect of, an enlargement or contraction of the bank circulation.[1]

The touchstone of a sound banking currency is redemption in standard coin on demand. A bank with authority to suspend coin redemption and with no limit upon its issues is in the position of an individual authorized to write notes

[1] Quoted by Mill, B. III., Ch. xxiv., Sec. 1.

and contract debts without any obligation to keep them related to his purse and property. Redemption in coin on demand constitutes the essential soundness of a banking currency and keeps a bank tied strictly, even if there is no limit of law upon its note issues, to its available assets. A bank should, therefore, keep a coin reserve constantly in its vaults to pay depositors who desire coin and to redeem its circulating notes. This proportion is sometimes reckoned at one-third of the demand liabilities, but is often permitted by law to be less and is often required by prudent banking to be more. "The intensity of the liability," in the language of Mr. Bagehot, is to be considered as well as the amount, and "the cardinal rule is, that errors of excess are innocuous, but errors of defect are destructive." [1]

But a bank must have other quick assets than its coin reserve, for if it keeps too large a proportion of its assets in idle coin it will make no profit, and if it keeps too large a proportion in investments which cannot be quickly turned into cash it will have no means of replenishing its reserve in case of necessity. The demands of a crisis or even a temporary change in the financial situation often make it necessary for a banking institution to redeem a large part of its note issues in cash, to pay off depositors in cash, and to contract at once the volume of its issues and its discounts. The character of these obligations requires that banks of issue should deal almost exclusively in commercial paper running for short terms. So long as universal insolvency is averted, the holding of such paper—running in most banking systems no longer than three months—affords the bank an

[1] *Lombard Street*, Works, V., 195, 208. It may prove advisable to concentrate the actual coin holdings in the hands of a few strong banks, whose notes are substituted for coin in redemptions by the smaller banks, but that is a question of detail which need not be considered here. The essential point is that there shall be an ultimate coin reserve somewhere, upon which the circulation of all the banks actually rests. In the English system the Bank of England holds the ultimate gold reserve of the entire country, and Bank of England notes are a legal tender everywhere but at the bank, where they must be redeemed in gold.

easy control over its resources and liabilities. If danger threatens by the diminution of the cash reserve, liabilities can be reduced by the restriction of new discounts until the reserve accumulates by the payment of maturing paper. If the terms of maturity are scanned with sufficient care to secure something like an even distribution day by day and week by week, the command of the bank over its resources is practically complete. The restriction of new discounts for a few days and the collection of maturing debt will change the relations between liabilities and assets at the same time that this policy acts in a broader way to reduce the outstanding circulation and influence the rates of foreign exchange.

The only safe rule for a bank of issue, which is compelled to redeem its notes in coin on demand, is to keep a large proportion of its assets in a form in which they can be quickly turned into cash. It is when this rule is violated by loans on doubtful paper, which have to be continued instead of being paid at maturity, or by loans on real estate and in industrial enterprises, which tie money up for long terms, that banks of issue find their cash exhausted and are driven into insolvency. Next in value to coin and commercial paper as quick assets, therefore, are good negotiable securities. These securities in ordinary times can be quickly sold without loss in the stock markets and turned into cash to swell the reserve. It is true that crises have occurred so acute that even the public stocks found for a moment no ready market, but these occasions have been the result of a temporary blind terror, against which the most perfect system of banking yet devised has not been sufficient to guard, and they have never lasted beyond a few days or weeks.[1]

[1] It was found in New York City in the panic of 1873 that loans on commercial paper for short terms were more available than loans on call or collateral. The call loans could not be paid by the brokers and the value of the stocks deposited as collateral shrunk so rapidly that they could not be sold for enough to cover the loans. The credit of the makers of commercial paper stood the strain better and their obligations were found more valuable for the moment than those of the brokers.—Bolles, III., 349–50.

The necessity of redeeming notes on demand is the reason why no currency based upon land or property has ever been kept permanently at par with coin. Mortgage banks and finance companies are legitimate forms of business enterprise, but they are not capable of doing the business of a bank of issue. The assets are available only at long intervals and cannot be quickly converted into cash in an emergency. Several of the leading banks of issue in Europe and many such banks in the United States do a certain amount of mortgage business, but it is usually limited to a small proportion of their aggregate transactions and in many cases is restricted by law to a fixed percentage of the capital. The two leading banking institutions of Belgium early in the present century and the banks of Italy and Australia more recently violated this rule of separating their note issue business from their long term loans and were forced to the suspension of specie payments as the result.[1]

The necessity of redemption of bank-notes in coin on demand is closely related to the regulation of the volume of the currency and a stable system of values. A surplus of redeemable bank currency instantly corrects itself. Depositors who found themselves burdened with surplus bank-notes would take them to the bank for transfer to their deposit accounts. Those issued by the depositor's bank would be covered into its own vaults and could not be issued again in any case until there was a demand for loans and discounts. Those of other banks would be returned to them, under any proper law, for redemption. This would be done by clearing-house arrangements, which might not in every case call for

[1] M. Courcelle-Seneuil (211) very properly suggests that "when a bank of circulation is well established, it may consider its minimum of circulation as a permanent deposit and make investments for long terms with the capital of this deposit." Where reasonable confidence exists in the banking system, the coin reserve is much more likely to be drawn upon by the withdrawal of deposits than by the direct presentation of notes for redemption, and this has to be reckoned with by the banker. What is stated in the text is, of course, only the outline of the theory of a banking currency and is subject to many modifications consonant with sound banking.

transfers of coin, but would in every case involve the return of the notes to the issuing bank and their withdrawal from circulation. The currency would be promptly contracted, without the expression of any distrust by the business community and without even the knowledge by an individual depositor of bank-notes that others as well as himself found their supply of bank-notes in hand larger than usual. The operation would, indeed, be so completely automatic that the redundancy could never reach any considerable proportion of the outstanding issues and an unusual issue of currency in response to a special demand would be promptly followed by contraction, when the demand ceased, without intentional concert of action or any change in the usual practices of the business community. If a crisis were conceivable which made the currency so redundant as to arouse distrust, the banks themselves would become the most powerful agencies in bringing it again within the proper limits. If they found their notes coming in not only for deposit, but for redemption in coin, they would take immediate measures to restrict issues and husband their coin. If they had been slow in forwarding the notes of other banks for redemption, they would forward them promptly when the accumulation became rapid, and if they had been indifferent about demanding settlement of balances in standard coin, they would insist upon that right.

The requirement of a sound banking currency, that the notes issued shall be redeemable in standard coin on demand, has another purpose than the mere test of the solvency of the banks. It goes to the foundation of the economic and financial system of the country and regulates its commercial relations with other countries. This result is reached through the medium of foreign exchange, which operates to maintain an equality of distribution of money among different communities and to keep their merchandise markets in touch with each other. Metallic money is the money of the world and of international exchange. A redundancy in one country brings about changes in the condition of the loan market which correct the redundancy and have an influence upon

interest and prices. It is not necessary to maintain the old theory that prices are governed by the volume of metallic money or credit paper in order to show that a redundancy of the circulating medium corrects itself through the foreign exchanges. As John Stuart Mill acutely remarked a generation ago, when this subject was less clearly understood than at present: "It is a fact now beginning to be recognized, that the passage of the precious metals from country to country is determined much more than was formerly supposed, by the state of the loan market in different countries, and much less by the state of prices."[1]

It is only within the last half-century that the manner of controlling the exchanges has come to be thoroughly understood. It is necessary, to a proper understanding of the subject, to treat metallic money as a commodity and to apply to it the laws of supply and demand which govern other commodities. In the words of Professor MacLeod:

"Discounting a bill for a merchant is not *lending* him money but *buying* a debt due to him: and the price of such debt must follow exactly the same laws as the price of corn, or any other article. If money is very scarce, and wheat very abundant, the price of wheat must fall; if money is very abundant, the price of wheat will rise. The price of debts obeys the same rules. If money becomes very scarce, the price of debts must fall, *i.e.*, the discount must rise. If specie becomes abundant, the price of debts will rise, *i.e.*, the discount will fall. The price of debts, then, must follow the same great laws of nature that the price of wheat does."[2]

This proposition, simple enough to the modern banking community, was only imperfectly understood and tardily acted upon down to 1860. The Bank of England then for the first time, at the suggestion of Mr. Goschen, adopted the principle of sharply raising the rate of discount one per cent. at a time when gold began to leave the country. The effect was marvellous and the method then adopted has since been followed, with more or less halting steps, by every banking institution in the world when it has been threatened

[1] *Political Economy*, B. III., Ch. viii., Sec. 4.

[2] *Theory and Practice of Banking*, II., 278.

by a drain of bullion. The effect of offering a higher price for money is to attract money while compelling the sale of commodities. It is not so much that commodities fall because the mere volume of the circulating medium has been reduced, according to the theory of the classical school of political economy. It is rather because the price of money having been raised by those who have it to sell in the form of loans, the manufacturer or owner of merchandise prefers to sell his goods at a reduced price rather than pay the higher rate of discount for continued accommodation at the bank.

The folly of attempting to maintain a uniform rate of interest or discount is on a par with maintaining a uniform price of wheat. At times the price would be too high and the wheat of the world would glut the markets of the country enforcing such a law, diverting the capital which might have been expended for other commodities and resulting in artificial relations between wheat and all other articles. At other times the price would be too low and wheat would flow steadily to the countries paying the market price, while starvation would stalk through the country which maintained a fixed legal price. Money is governed by exactly the same laws. The attempt to maintain a uniform rate of interest or discount would result in some cases in a glut of bullion, when the ruling rate of the world was lower, which would be as real an inflation and as unhealthy an expansion of credit as any form of paper inflation; it would result in other cases, when the ruling rate of the world was higher, in the withdrawal of all the bullion which a country possessed.

A banking currency, regulated by sound laws and the enlightened experience of modern banking, affords as perfect a regulator of the monetary circulation as the automatic governor of a steam engine. When capital is redundant, it flows into the banks in the form of deposits of bank-notes and of coin. The bank-notes are cancelled and retired and if the redundancy of capital continues the rate of discount falls and the surplus is available for domestic or foreign investments. Domestic industry is thus able to revive after

a commercial crisis as the result of the low rates for idle capital. The surplus of currency which is not thus absorbed goes abroad in the form of bullion. The moment such losses of bullion go too far and put a strain upon the coin reserves of the banks, their rate of discount is raised. This has the triple effect of retaining capital at home which would otherwise be exported, attracting capital from abroad, and putting a check upon speculative enterprises upon small margins. Money becomes harder to get and it is not gotten for so many doubtful enterprises or for those promising small and distant returns.

Money and capital are regulated by the law of supply and demand, like other commodities. They pay smaller percentages of profit, as a rule, than other commodities and there is no danger that they can be cornered or monopolized. Capital is a generic thing which can be acquired by any one who saves. In this it differs from specific commodities, which may require special methods of production and which can be made the subjects of monopoly. The conception which has sometimes taken possession of the opponents of a banking currency, that capital and money can be "cornered," is an absolute chimera under a system of free banking. Banking systems have been in force which have had a tendency to restrict the supply of money because of the conditions they imposed upon the quick conversion of capital into negotiable form ; but just so far as a banking system is free it escapes the possibility of such an evil, whatever others it may bring in its train. The theory that all bankers and persons capable of becoming bankers could or would form a combination to raise the value of money when it was plentiful is the same in substance, and is as reasonable, as the theory that all holders of capital would cease to make promissory notes, draw checks, and grant credits on their books. The form which this theory usually takes, that a banking currency would encourage the " cornering " of money more than a government paper currency, is peculiarly ill-considered, because the amount of the latter is fixed and cannot be increased without awaiting the slow process of legislative action, which

usually involves also the suspension of specie payments and the upsetting of the standards of value. The only way of "cornering" money is by raising the interest rate. The moment this rate was raised above that fixed by free competition in the markets of the world, foreign capital would pour into the country where this condition existed in a golden stream of coin and bullion, interest rates would begin to fall again, and the "corner" would more quickly collapse than has ever been the case in the wheat or cotton market.

It is not to be inferred from what has preceded that no regulation of banks of issue by law is justified or required. The theory of free banking simply assumes that equal privileges shall be granted to all banks which comply with uniform and reasonable conditions. The contest which has been waged in France and some other European countries on behalf of free banking has not been waged against proper government supervision of banks of issue, but against the grant of the privilege of monopoly of issues to a single institution or a limited number of institutions. Government regulation of institutions owned entirely by private individuals is a very different thing from government ownership, and the exercise of such supervision under a banking system open to all comers who comply with reasonable requirements is very different from its exercise over a single institution, holding special privileges by grant of the sovereign power. The essential limitation upon government supervision of banking is that it shall restrict as little as possible, consonant with the safety of the business public, the full operation of the functions of the bank. It may be justifiable to impose fixed proportions between capital and note issues and between liabilities and the normal cash reserve; to provide specific methods of keeping accounts and to authorize full government inspection of such accounts; but legal regulation should allow as much elasticity as possible in the full use of the powers of the bank in times of emergency for the accommodation of solvent business men and the protection of the community from needless panics.

CHAPTER II.

ANCIENT AND MODERN BANKING IN ITALY.

Character of the Ancient Banks—Origin of the Word "Bank"—The Banks of the Italian States—The Unification of the Banking System—The Paper Money Mania and the Present Economic Condition of Italy—Flight of Subsidiary Silver to Other Countries.

ITALY is in a sense the mother of modern banking, as she is also the inspiration of much that is best in modern literature, art, and religious faith. The oldest bank is generally considered to have been that of Venice, founded during the wars which the island republic was waging with the Roman Empire of the East and its successor and rival, the Holy Roman Empire of the West. The Bank of Venice, however, was at the outset simply a transfer office for the national debt. Several forced loans had been contracted, the first apparently in 1156, which were converted into perpetual annuities, paying an annual interest. The government appointed commissioners to consolidate these loans and to issue stock certificates or credits. This constituted the evidences of the debt into registered negotiable securities, which were transferred from time to time on the books of the bank and thus served certain purposes of exchange in the same manner that such securities serve at the present time. The actual business of deposit banking by the issue of circulating notes was not undertaken by public authority in Venice until four centuries later, in 1587, when foreign coins were received at their bullion value and certificates were issued promising a return of bullion of

the same value of standard weight and fineness.[1] The Bank of Venice proper (*Banco del Giro*) was established by decree of the senate in 1619.[2] The origin of the word "Bank," is traceable, however, to the form of business done by the Venetian loan office, and for this reason it deserves some attention as the origin of modern banking.

One of the names of a public loan in Italy was *Monte*, or joint-stock fund, and the first Venetian loan was called the *Monte Vecchio*, or old loan, in contrast with the later ones, called *Monte Nuovo*, and *Monte Nuovissimo* (new and newest). The Germans were influential in Italy at this time and their word for *Monte* was *Banck*, which the Italians converted into *Banco*. The word bank was frequently used in English as well as Italian to signify a mass of money or a joint stock fund. The definition given in an Italian dictionary in 1659 is, "*Monte*, a standing bank or mount of money, as they have in divers cities of Italy."[3] The issue of paper money directly by the state was spoken of as "raising a Banke" in colonial days in Massachusetts, the word, "bank," standing for the money rather than the institution which put it in circulation.[4] Blackstone also says that at Florence in 1344, "government then owed about £60,000, and being unable to pay it, formed the principal into an aggregate sum, called, metaphorically a *Mount* or *Bank*, the shares whereof were transferable, like our stocks."[5] The use of the word, therefore, if not the methods of modern banking, comes from the institutions of Venice, Florence and Genoa, which were at the outset the registry offices of the public debt.

The Bank of Genoa grew out of the pledge of the public revenues for the loans contracted to carry on the wars of the fourteenth century. The lenders were permitted to receive the produce of the taxes by their own collectors, paying into

[1] Gilbart, I., 11, note.
[2] Palgrave, 103.
[3] MacLeod, *Theory and Practice of Banking*, I., 315.
[4] Weeden, 318.
[5] *Commentaries*, I., 327.

the Treasury the excess above their claims. The multiplicity of these claims led to the formation in 1407 of the Bank of St. George, which became from that time the sole intermediary between the State and its creditors. Every senator on taking office swore to maintain the privileges of the bank, which were confirmed by the Pope and the German Emperor. "The bank," says Hallam, "interposed its advice in every measure of government and generally, it is admitted, to the public advantage. It equipped armaments at its own expense, one of which subdued the island of Corsica; and this acquisition, like those of our great Indian corporation, was long subject to a company of merchants, without any interference of the mother country."[1] This territory was taken by way of security for the loan, in the same manner that revenues from specific sources are still pledged by second-rate powers in Europe and Asia for the fulfilment of their pledges.

The forerunners of modern loan and deposit banks were the private bankers of the Italian cities who lent money to traders, merchants, and kings. The Jews were the money lenders of the dark ages and their monopoly of the business was confirmed among the Christians by an absurd prejudice against lending money at interest, upon the ground that it constituted usury.[2] The Jews were several times expelled from the leading countries of Western Europe, and as early as the thirteenth century the Christian merchants of Lom-

[1] *Europe during the Middle Ages*, II., 530.

[2] Prof. Jannet points out that the prejudice against loans at interest was not without its justification before money came to be borrowed for the purposes of production, because the proceeds of the loan were usually consumed instead of multiplied, and if loans at interest had been universally approved they would soon have resulted in rural localities in the practical enslavement of the peasants who were unable to pay. The distinction between loans for production and for consumption was early recognized by the Church, and the fifth Lateran Council (1512-17) decreed: "Ea est propria usurarum interpretatio, quando videlicet ex usu rei *quae non germinat* nullo labore, nullo sumptu, nullove periculo lucrum foetusque conquiri studetur."—*Le Capital, la Spéculation, et la Finance*, 81.

bardy and the South of France took up the business of remitting money by bills of exchange and of lending at interest. Bills of exchange proved peculiarly useful to the Church of Rome by facilitating the remission to Italy of the immense sums subscribed by the faithful beyond the Alps, and Italian bankers penetrated to England and were allowed to farm the customs as security for their loans.[1] Edward III. defaulted in his payments, owing the Bardi at Florence 900,000 gold florins, and the Peruzzi 600,000 florins. These two great banking houses, who were described by Villani as the pillars which sustained a great part of the commerce of Christendom, were obliged to suspend, and their failure carried down a great number of Florentine citizens and caused great distress in the city.

The essential feature of modern banks of issue—the circulation of notes payable to bearer and redeemable in coin, but only partly covered by the coin reserve,—was not worked out until the seventeenth century. The famous Bank of Amsterdam, founded in 1609, was—like the Bank of Venice, after it really became a bank at all,—a mere issuer of warehouse receipts for coin. The foundations of the great structure of modern credit were already being laid among private citizens and money lenders, but had not attained their present form. That property might be transferred by paper representatives was demonstrated by the immemorial use of bills of exchange, and the perception of this truth led to the many crude schemes of banking upon landed security which formed the basis of Law's bubble under the French monarchy, led the American colonies through every form of monetary folly, and deceived for a moment even the sane, clear mind of Hamilton. William Potter, in his *Key to Wealth*,[2] groped towards the modern theory of bank issues in the suggestion that greater mobility should be given to trade by some firm and known security

[1] Hallam, II., 529. The Bardi are said to have farmed all the customs in England in 1329 for £20 per day.

[2] Published in London in 1650.

and that, failing a new supply of gold and silver, a flag or sign of specie might be instituted. He grasped the conception of some of the best modern thinkers in the statement that "Money is given to men for their commodities, upon no other accompt than as an *Evidence* or *Testimony* (That is as it were a Token or Ticket) to signifie how far forth other men are indebted for, and ingaged to recompence the fruits of their labors, or possessions by commodities of some other kind, instead of those that for such money they parted with." China had paper money as early as the seventh century, but the transport notes of the Stockholm bank, issued in 1661 to avoid the transportation of copper coin, are considered the earliest type of modern bank-notes.[1] With the progress of the arts of peace, the private bankers, the great banks of Italy, and the Bank of Amsterdam thus gradually perfected the methods of clearing by credits on their books, while the great incorporated banks provided credit with its potent modern instrument—the bank-note payable in coin on demand.

But it is the purpose of this work to deal with modern banks of issue and not with the antiquities of mediæval commerce. The disorders which came on the heels of the French Revolution, wiping out the boundaries of states and destroying the freedom of the Italian cities, put an end also to most of the ancient banks. The only one which survived was a land and mortgage bank called *Monte dei Paschi*, at Sienna, which was believed to date back to the seventeenth century. The first effort to found a modern bank was made at Genoa upon the foundations of the old Bank of St. George. The effort was not successful, and, in the opinion of M. Courcelle-Seneuil, this is not to be regretted, "for the Bank of St. George was adapted to customs and commercial usages which have ceased to exist." The next attempt to establish a banking system in Piedmont was made by letters patent of King Charles Albert, under date of March 16, 1844. The new bank was to be known as the Bank of Genoa, to have a

[1] Roscher, I., 443.

capital of 4,000,000 lires ($800,000), and to be under the supervision of a royal commissioner and sub-commissioner. The bank received a subvention of 4,000,000 lires from the government during 1846 and the following years, upon which it paid interest at two per cent. A bank was founded at Turin on October 16, 1847, with a capital of 4,000,000 lires, but the political and economic crisis of 1848 checked its development. A royal ordinance of December 14, 1849, authorized it to unite with the older bank under the denomination of the National Bank of Sardinia, with head offices at both Genoa and Turin. The duration of the new establishment was fixed at thirty years, beginning on January 1, 1850, and its capital at 8,000,000 lires, which was afterwards increased to 32,000,000 lires ($6,200,000).

The government in 1848 resolved upon a loan of 20,000,000 lires, which the Bank of Genoa was required to furnish at two per cent., upon the pledge of the goods of the Order of Saints Maurice and Lazarus. Forced legal tender character was given to the bank-notes and an increase in issues permitted of 20,000,000 lires. The smallest notes were reduced from 250 lires ($50) to 100 lires ($20) with the condition that the notes of 100 lires should not be issued to the amount of more than one-fifth of the total circulation. The loan was reimbursed to the bank and specie payments were resumed at the end of 1849.[1] The bank from that time followed the fortunes of the Royal House of Sardinia, and extended its branches and operations with the success of the Sardinian arms and the consolidation of the Italian States. It was necessary in 1856 to authorize the bank to exceed the maximum note circulation allowed by its statutes, which was three times the cash reserve. The bills of the bank were again made legal tender, with suspension of cash payments on April 27, 1859, on the occasion of the war with Austria, and the bank was authorized to issue 6,000,000 lires in notes of twenty lires ($4) and to open a credit for the government to the amount of 30,000,000 lires at two per cent. The bank

[1] Courcelle-Seneuil, 354.

was prudently conducted, the government did not draw its full credit, and the notes fell but little below par. Their circulation was extended on June 11, 1859, to the entire territory occupied by the Sardinian troops.

The bank was reorganized at this time as the National Bank of the Kingdom of Italy, in pursuance of the plans of King Victor Emmanuel for the unification of Italy. Its capital was increased to 40,000,000 lires ($8,000,000) and three head offices of equal rank were established at Turin, Genoa, and Milan, the latter being a new office within the territory added to the new Kingdom of Italy. The bank resumed specie payments and opened a credit of 18,000,000 lires in favor of the government. Branches were established in 1860 at Bergama, Brescia, Como, Modena, and afterwards at Ancona and Perusia. The bank absorbed the leading banks of Bologna and Parma and established branches at Ferrara, at Forli, and at Ravenna. The annexation of Naples to the Kingdom of Italy did not result in the destruction of the Banks of Naples and Sicily, but the National Bank was authorized to establish a principal branch at Naples and branches at Catana, Messina, Reggio, and other places in Southern Italy. Branches were also authorized at this time at Pavia, Cremona, and Piacentia.

The character of the National Bank of the Kingdom of Italy was not essentially changed until the Act of August 10, 1893, but its relations to the government constantly grew closer and it was compelled to accept forced legal tender for its notes in order to comply with demands for advances to the State. Suspension of specie payments was decreed at the outbreak of the war in 1866, although the capital of the Bank had been increased by the decree of June 29, 1865, to 100,000,000 lires ($20,000,000). The provision for the suspension of specie payments, with legal tender quality for the bank-notes, applied only to the National Bank, but the latter was required to furnish circulating notes without charge to other banks of circulation. The depreciation of the bank-notes drove the subsidiary coins out of circulation, and many small banks of deposit, commercial houses, and even retailers, issued

certificates of one lire and 50 centimes to take their place. The government in 1868 sought to drive these notes out of circulation by authorizing the issue of notes for one lire by the regular banks of circulation, which were made legal tender for a limited sum throughout the Kingdom. The bank made handsome profits, as usual when specie payments are suspended, made large advances to the government and again increased its capital to 200,000,000 lires under authority of a law of April 9, 1872.[1]

The policy of the Italian government to introduce unity into every branch of Italian affairs was pursued cautiously in the case of the bank-note circulation and without the hasty abrogation of the rights of the banks. No new bank could be constituted without the authority of a special law, but five banks of circulation conducted business without interference by the side of the National Bank of Italy. The Roman Bank, founded in 1851 with a privilege secured until December 31, 1889, had a capital of 15,000,000 lires and while Rome was independent of the Kingdom of Italy was under the protection in a measure of the Papal power. The National Bank of Tuscany was established in July, 1857, with a capital of 30,000,000 lires and the Tuscan Bank of Credit was established for thirty years in March, 1860, with a capital of 10,000,000 lires, of which only half was paid in. Both these banks were located at Florence. The Bank of Naples was founded as early as 1794 and the capital was contributed in part by the State. It had a head office at Rome and about a dozen branches. The Bank of Sicily was also an old establishment, with its headquarters at Palermo, four principal offices in other parts of Sicily and branches at Rome and elsewhere in Italy. The capital of the Bank of Naples was originally 32,500,000 lires and that of the Bank of Sicily was 8,000,000 lires. The authorized circulation of these banks under the law of 1874 was 450,000,000 lires for the National Bank of Italy ; 45,000,000 lires for the Roman Bank ; 63,000,000 lires for the National Bank of Tuscany ;

[1] Juglar, Article " Banques," in *Dictionnaire des Finances*, I., 344.

15,000,000 lires for the Tuscan Bank of Credit; 146,250,000 lires for the Bank of Naples, and 36,000,000 for the Bank of Sicily, making a total of 755,250,000 lires ($150,000,000).[1]

The necessity of maintaining public credit, and some complaints by the other banks that they suffered by the special favors granted to the National Bank, led to legislation in 1874 which established the Consorzio. This arrangement formed the banks into a syndicate for the withdrawal of the notes issued directly on behalf of the government and the substitution of a like sum (840,000,000 lires) in bank bills of the National Bank, which were made legal tender throughout the Kingdom. The notes issued by the provincial banks on their own account were to be legal tender only within the province in which the bank was established. The government voted itself the authority to increase its loans from the associated banks to 1,000,000,000 lires ($200,000,000) and to demand a certain proportion of the amount in gold. The government pledged itself to deposit five per cent. securities as the guarantee of the loan and to pay a low rate of interest. The advances actually made to the government under this arrangement reached 940,000,000 lires, of which 600,000,000 was reimbursed from the product of a specie loan authorized by the law of April 7, 1881, and the remainder was transformed into government bills. The Consorzio came to an end with the abolition of forced legal tender in 1884. The circulation of the banks was slightly increased by the law of June 30, 1891, which admitted a maximum limit equal to the mean circulation of 1890.

The suspension of specie payments, the failure of the Roman Bank, and the almost complete collapse of the banking system of Italy came about in the latter part of 1892 and the beginning of 1893 as the result of wilful violations of law by the banks and the guilty connivance of public officials. The Roman Bank was accused of exceeding its circulation at almost the same moment that the director of the Roman branch of the Bank of Naples, Signor Cucciniello,

[1] Alfred Neymarck, Article "Banque," in *Dictionnaire d'Économie Politique*, I., 141–42.

fled with his secretary, leaving obligations of 2,000,000 lires ($400,000) and compelling the branch to close. It was found that the excess of note issues had been distributed among the politicians by the thousands and hundreds of thousands. A Roman deputy had received 4,000,000 lires; a former minister, 2,000,000 lires; a well-known financier, 1,500,000; a newly elected deputy, 1,000,000; a former editor, 150,000; and others, various sums from 1,000 to 500,000 lires.[1] Some of these sums were put in the form of loans and advances, but the security was nominal, many of the loans were long over-due, and Signor Tanglongo of the bank management declared that he had been compelled to retain these people by the orders of several ministers and of a president of the council.

An official investigation was ordered and the report by Senator Finali showed that three of the banks had exceeded the legal limit of their circulation and that all had tied up their assets to an alarming extent in securities which could not be readily negotiated. The excess of circulation in the case of the Roman Bank was 64,543,230 lires; the Bank of Sicily, 14,917,203 lires; and the Bank of Naples, 2,041,501 lires. It was found that the National Bank also had issued 53,700,000 lires illegally by order of the administration. The funds not readily negotiable at sight were reported as 628,620,686 lires, or nearly twice the capital and reserves of the banks, the Tuscan Bank of Credit alone being in a sound condition.[2] The loans upon mortgages and other securities slow to realize were 199,756,000 lires, and what were called the "Direct Employments" of the funds, in Treasury bonds and other paper below par or of doubtful value, were 172,343,000 lires. The deputies who had paper over-due were found to number sixteen, and the amount of the paper was 5,922,410 lires, some of it going back to 1878. There were nine more deputies who had obtained renewals to the amount of 641,670 lires. Among the latter was Premier Crispi, with loans of 244,000 lires which had been renewed since 1887.

[1] *Revue des Banques*, March, 1893, XII., 335.

[2] *Revue des Banques*, May, 1893, XII., 378.

It was stated that a report of August 30, 1889, had shown a clandestine circulation of 9,000,000 lires by the Roman Bank, and that it was known to Signor Crispi, then President of the Council of Ministers, as well as to Signor Giolitti.[1]

These discoveries were a death-blow to the Italian banking system as it then existed. The Roman Bank was compelled to liquidate, and its affairs were taken in charge by the National Bank. The privilege of the banks expired in 1889 and 1890, but had been renewed for brief periods until the close of 1892. A law was then pending, proposed by Signor Grimaldi, which provided for a renewal for six years, and that every bank should accept the notes of the others. But this project went by the board when the rottenness of the existing banking system was discovered, and the government seized the opportunity to push a step further the policy of unity and consolidation. The National Bank of the Kingdom was badly compromised, and the redemption of its notes in specie was indefinitely suspended, but it was made the basis of the new institution founded by the law of August 10, 1893.

The new law provided for the fusion of the National Bank of the Kingdom of Italy with the National Bank of Tuscany and the Tuscan Bank of Credit. The name of the new institution is simply the Bank of Italy, and it is required to establish offices or branches wherever they have been established by the National Bank of Tuscany. The capital of the new bank was fixed at 300,000,000 lires ($60,000,000) and its privileges were confirmed for twenty years. The Roman Bank was already in process of liquidation when this act was passed, so that the only remaining banks of issue are those of Naples and Sicily. The maximum limit of circulation during the continuance of the forced legal tender policy, was fixed at 800,000,000 lires for the Bank of Italy, 242,000,000 lires for the Bank of Naples, and 55,000,000 lires for the Bank of Sicily. This circulation is to be reduced every two years after 1897, and until in 1907 it shall stand

[1] *Le Marché Financier en 1893–94*, 131.

at 630,000,000 lires for the Bank of Italy, 190,000,000 for the Bank of Naples, and 44,000,000 lires for the Bank of Sicily, making a total of 864,000,000 lires. If either bank at the end of fourteen years, from the date of the law, lacks a reserve corresponding to one-third of its circulation, the circulation must be reduced within three months, and the amount of the reduction transferred to the banks which possess or pay in the necessary reserve.[1] The banks are authorized to increase their circulation beyond the legal limits when their notes are entirely covered by legal coin or by gold bullion, and notes may be issued beyond the limit for the purpose of advances to the government.

The reserves of the banks, when on a specie basis, are fixed at forty per cent. of the circulation, including thirty-three per cent. in coin or bullion and the remainder in foreign bills of exchange approved by the Minister of the Treasury. The metallic reserve is required to consist of gold in the proportion of at least three-quarters. The law provides that bills now in circulation shall cease to be a legal tender after December 31, 1897, and shall no longer be redeemable after December 31, 1902. A permanent supervision over banks of issue is established through a board consisting of the Minister of Agriculture, Industry and Commerce, and the Minister of the Treasury. A special inspection is to be made under the authority of these ministers every two years, and the results reported to Parliament within three months. The nomination of the director general of the Bank of Italy must be approved by the government. One of the provisions of the law provided that if the deposits exceeded a certain figure, the bank must reduce its circulation by three-quarters of the deposits bearing interest in excess of the limit; but this provision was suspended by decree of January 23, 1894.[2]

The new banking law did not rescue Italy from the *régime* of depreciated currency and was probably not expected to do so. The government was reduced to subterfuges to in-

[1] Section 2, Law of August 10, 1893, *Bulletin de Statistique*, XXXIV., 254.

[2] *Bulletin de Statistique*, February, 1894, XXXV., 207.

crease the volume of paper money and provide itself with funds to meet pressing obligations. The decree of January 23, 1894, permitted a supplementary issue of bank-notes to the amount of 90,000,000 lires for the Bank of Italy, 28,000,000 for the Bank of Naples, and 7,000,000 for the Bank of Sicily. These new issues were not directly authorized, but the penal tax imposed by the banking law was reduced to two-thirds of the rate of discount up to the limit of the proposed new issue. A decree a month later, February 21, 1894, purported to put a limit of 600,000,000 lires on the circulation of State notes, and Article 5 of the same decree provided that the banks might redeem their notes on presentation at the market rate of depreciation. This favor was only to be accorded, however, to the banks which complied with the requirement of Article 2, that they transfer to the credit of the government 200,000,000 lires in gold and accept a new issue of government notes as a substitute.[1] The new notes, of which 145,000,000 lires were apportioned to the Bank of Italy, 45,000,000 lires to the Bank of Naples, and 10,000,000 lires to the Bank of Sicily, were thus nominally covered by gold, but no provision was made for reducing the volume of outstanding bank-notes or for replacing the gold withdrawn from the bank reserves.

The result of measures like these was to drag Italy deeper and deeper into the mire, make the rates of foreign exchange more and more unfavorable and the receipts of the Treasury of constantly diminishing value in gold. The additional issue of bank-notes authorized by the decree of January 23, 1894, was avowedly for the purpose of meeting the demands of the depositors in the savings banks, who upon demanding the restoration of the deposits they had made in good money were reduced to the choice of leaving their deposits in the hands of a discredited government or accepting the paper promises of the suspended banks. One of the expedients adopted to protect the Treasury was the levy of a tax of twenty per cent. on the interest of the public debt, which was

[1] *Bulletin de Statistique*, March, 1894, XXXV., 335.

only an indirect way of scaling the interest on the consolidated five per cents. to four per cent.[1] The depreciation of the paper money has become so great as to drive all subsidiary coins out of the country and make it difficult to get change for a note of a few lires. Twenty million lires was issued during 1894 in nickel pieces of twenty centimes, and the government congratulated themselves on a profit of 17,500,000 lires by means of the seignorage.

The flight of subsidiary money from Italy carried it to France, Switzerland, and, to some extent, to Belgium, where it passed in ordinary transactions upon the same terms as the money of those countries. So much Italian silver drifted into Southern France that the French government made an investigation of the amount received on a given day at some of the leading banks and found that Italian pieces constituted 28.78 per cent. of the entire subsidiary circulation. Belgian, Swiss, and Greek pieces constituted 12.30 per cent., so that the proportion of French coins was only 58.92 per cent. Italian subsidiary coin constituted more than seventy per cent. of the circulation in Savoie and the Maritime Alps and from 45 to 60 per cent. in eight other departments between the Rhone and the Alps.[2] A conference of the states of the Latin Union, held at Paris, reached an agreement on November 15, 1893, by which the Italian subsidiary coins were to cease in four months to be received by public depositaries in France. Those in the Bank of France were, upon presentation to the Italian government, to be redeemed half in gold and half by bills of exchange. The amount thus presented up to the close of 1894 was 57,222,279 lires.[3] The policy adopted by the Italian government for preventing the continued exportation of the silver, of locking it up in the Treasury and issuing small notes against it, was sanctioned by the conference upon the condition that the subsidiary

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[1] *Le Marché Financier en 1893–94*, 136.

[2] *Le Marché Financier en 1893–94*, 348–68.

[3] *Assemblée Générale des Actionnaires de la Banque de France du 31 Janvier, 1895*, p. 9.

silver of Italy should never exceed the limit of six lires per head originally fixed by the Latin Union.

The report of the Minister of the Treasury, Sidney Sonnino, to the Chamber of Deputies, on December 10, 1894, offered only a distant hope of the restoration of sound financial conditions in Italy. The result of the special examination of the banks in February was, in his own words, "not very favorable." The Minister proposed a somewhat elaborate scheme of law to put in effect a convention between the bank and the Treasury. The period of liquidating the unavailable assets of all the banks was extended to fifteen years. The Bank of Italy assumed the liquidation of the affairs of the Roman Bank and received in return the custody of the public funds in the provinces, paying interest at one and a half per cent. on sums above 40,000,000 lires. The bank was required to deposit with the Treasury a guarantee fund of 50,000,000 lires in national securities and to increase the amount within six years to 90,000,000 lires; to increase the limit of advances to the Treasury from 90,000,000 to 100,000,000 lires; to call upon shareholders for an assessment of 100 lires per share, amounting to 30,000,000 lires, and to reduce the capital by an equal amount. The bank was required to set aside 4,000,000 lires in 1894, 5,000,000 lires in 1895, and thereafter 6,000,000 lires annually, to be invested in national securities to form a reserve fund to cover the losses by the Roman Bank, and any profit which might remain was allowed to be divided among the shareholders, to a maximum limit of 40 lires per share.[1] This remarkable method of liquidation,—by converting locked-up assets into a new form of such assets, instead of paying off liabilities,—was approved by the shareholders of the Bank of Italy on February 25, 1895, for they practically had no option but to accept the proposals of the government.[2]

The following table shows the condition of the three Italian banks of circulation on September 30, 1895:

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[1] *Bulletin de Statistique*, December, 1894, XXXVI., 587–89.

[2] Raffalovich, *Le Marché Financier en 1894–95*, 177.

BANK.	METALLIC RESERVE.	CIRCULATION.	CURRENT ACCOUNTS.	DISCOUNTS.
	(In millions of lires.)			
Bank of Italy.....	349.7	766.9	229.8	208.6
Bank of Naples...	116.1	238.7	78.6	53.8
Bank of Sicily....	36.7	49.2	36.4	22.0

One of the beneficent features of the banking system of Southern Italy is the support which it lends to the popular banks, which afford a means of raising money to small cultivators, shopkeepers, and even to laborers. The government was empowered, by Article 38 of the law of January 23, 1887, relating to people's banks, to authorize loans for agricultural purposes by banks of issue. The necessity of using this power sparingly was appreciated, but the management of the Bank of Naples voted on May 4, 1889, to set aside 8,000,000 lires ($1,600,000) for this purpose and their action was approved by the government.[1] But perhaps the more important service rendered to popular credit is in the rediscounting of the paper of the people's banks. The large bank thus escapes the difficult work of discriminating among individuals of small means by directly discounting their paper and obtains at the same time the guarantee of the local bank as well as of the borrower and his security. The Bank of Naples voluntarily discounts for those who appear most worthy of it at one per cent. below the ordinary commercial rate. Thirty-four people's banks in 1883 had obtained this reduced rate on sums of 4,249,348 lires ($820,000) and thirty-six banks had obtained discount at the regular rates on 9,971,726 lires ($1,924,000).

The Bank of Sicily has endeavored even more generously to promote the system of the people's banks. Signor Notarbartolo, the director general, proposed in 1882 the establishment of independent agencies, sharing in the profits of the Bank and supported by its credit; but the Minister of Agriculture and Commerce decided that a bank of issue could

[1] Durand, 481–82.

not receive additions in this manner to its capital without authority of law. Signor Notarbartolo then formulated a plan for making the people's banks correspondents of the Bank of Sicily with the benefit of discount one per cent. below the ordinary rate and this was put into actual operation.[1] The result has been the creation of popular banks all over Sicily and Southern Italy. The popular banks of Northern Italy had an older foundation and were either capable of standing alone or were sustained by other institutions which were not banks of issue.

[1] Durand, 509.

CHAPTER III.

BANKING IN FRANCE.

The Events Out of Which the Bank of France has Grown—The Mississippi Bubble of John Law and its Collapse—The Banks of Paris before the Revolution—Failure of the Assignats and the Revival of Commercial Banking—Birth of the Bank of France and its Absorption of the Departmental Banks—The Latin Union and the Embarrassments Caused by the Fall in the Price of Silver—The Proposed Renewal of the Bank Charter.

THE Bank of France is the greatest and in many respects the strongest of the banks of the world, and its development exhibits many of the most interesting phases of banking history outside of Great Britain. French banking is done pre-eminently through the issue of circulating notes, and the aggregate monetary circulation of France is greater than that of any other country. The origins of banking in France go back to the "Mississippi plan" of John Law, but its history during the present century has been essentially one of prudence and moderation, if not always of the most enlightened financial policy. Monopoly of the power of note issue now belongs to the Bank of France, but is far from having been its immemorial right. The *régime* of the independent departmental banks, which were absorbed by the central institution in 1848, is still recalled with pride by many French economists, and the approaching expiration of the charter of the Bank of France may tempt them to a renewal of the contest then so warmly waged between "monopoly" and "liberty."

The first French bank of issue was created by John Law under the regency of the Duke of Orleans, at the beginning

of the eighteenth century. Scotland, which gave to the world the founder of the classical school of political economy in Adam Smith, was also the birthplace of Law, the author of "The System" which introduced the use of negotiable securities on a broad scale into France. The name of Law has been synonymous with the most reckless speculation and brazen fraud, but the bank which he founded was at the outset conducted upon conservative principles, and even the system of the "Company of the West" (*Compagnie d' Occident*), more generally known as the Mississippi Company, was conceived upon broad and not impossible lines before the stock was made the plaything of speculation. Law desired to establish a royal bank of state, but the government was only willing to grant a charter for an institution managed by private citizens. The bank thus founded by letters patent May 2, 1716, was authorized to issue bills in crowns of specie under the name of "bank crowns," redeemable in money of the weight and denomination of the day of issue.[1] This was intended to guard the bank-notes against the possible fluctuations and changes in the metallic standard and give them some such preference as that given to the "bank money" of the Bank of Amsterdam. The feature which rapidly attracted subscriptions to the stock was Law's offer to accept payment at the rate of twenty-five per cent. in specie and seventy-five per cent. in bills of state, which were at a discount of about seventy-five per cent.

Discount was granted by the bank at the rate of five per cent., and officers of the finances received orders in October, 1716, to make their remittances upon Paris in bank-bills, and to redeem these bills at sight when presented to them. Another official decree of April 10, 1717, authorized the receipt of the bills as money for the payment of public revenues. If the bank had continued upon the sound basis of a bank discounting commercial paper and acting as the fiscal agent of the Treasury, France would have been under a great debt of gratitude to Law for introducing into her commercial relations the methods of the modern

[1] Courtois, 10.

business world. Prof. H. Dunning MacLeod, as keen a thinker and acute a critic as has written upon monetary subjects, says:

> Nothing could be more extraordinary than the restoration of prosperity caused by the foundation of Law's Bank in 1716. It is probably one of the most marvellous transitions from the depths of misery to the height of prosperity in so short a space of time in the annals of any nation. And, if Law had confined himself to that, he would have been one of the greatest benefactors any nation ever had.[1]

But Law had much more comprehensive schemes than the creation of a bank of discount. He determined to unite into a single great monopoly the various commercial companies which had been incorporated since the discovery of America, for the purpose of trade and the extension of French influence. Courtois enumerates no less than thirty of these corporations which had been authorized during the previous century, but many of them had languished, run in debt, and been consolidated with others. Law proposed a stock company with a capital of 100,000,000 livres, divided into 200,000 shares of 500 livres each, payable in bills of state which were still at a discount of about sixty-six per cent.[2] The State was to pay the company an annual interest of four per cent. on the principal of the bills withdrawn by this means from circulation.

The *Compagnie d'Occident* was incorporated by a decree of August 28, 1717, registered by the Parliament on September 6th, for a duration of twenty-five years. Four companies were consolidated at the outset, which controlled the commerce of Louisiana, Canada, and the Western Coast of Africa, and the new company was to enjoy all the rights of sovereignty over the lands which it possessed. The shares, which were made out in certificates of one share or ten,

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[1] *Theory and Practice of Banking*, II., 254.

[2] The variations in the coinage at this time were such as to make a statement of the value of coins an almost impossible task, but the livre may be taken in a general way as about the equivalent of the later franc—19.3 cents in United States gold coin. For a full account of the changes in the coinage system, see Shaw, 396–423.

were transferable by bearer, a system for the first time introduced into France, so far as known ; for even the shares of bank were made out to the owners. Law proceeded to make negotiations with the government through his friend, the Regent, for farming the taxes, for coining money, for managing the tobacco monopoly, which had been under the control of the State, and for assuming the entire public debt. He introduced a number of reforms into the collection of the taxes by discontinuing the collection of those which were disproportionately costly and vexatious in proportion to the amount obtained, and he proposed more sweeping changes which would have abolished needless offices, consolidated various imposts into one, and removed some of the fetters from French commerce.

The attribution of all these public functions to a single company, as well as the management of the commerce of two continents, would in themselves probably, as Law's great opponent, Paris-Duverney, pointed out, have caused the organization to break down of its own weight, and have attracted the jealousy of the government. But Law, and those who were carried away with him by the grandeur of the new scheme, did not wait for the slow operation of commercial causes to sow the seeds of destruction of their enterprise. He succeeded in having the bank transformed into a public institution (*Banque Royale*) by a decree of December 27, 1718, and had the stockholders reimbursed in specie for their subscriptions. Redemption of the notes in bank crowns was abandoned by the decree which made the bank a public one, and redemption was required only in the official money of the country. This move created a degree of distrust which led to a new decree of April 22, 1719, that bills payable in the existing standard should not be subject to the diminutions which might affect specie. The tendency of such a decree was to put the bank-bills at a premium over current coins, which were being perpetually debased and altered by the wretched administration of the finances. The total circulation of bills in April, 1719, the date of the last decree, was 110,000,000 livres ($22,000,000).

Meantime the shares of the *Compagnie d'Occident* were undergoing a remarkable experience. They were sold rather slowly at first and the principal subscription was by the former stockholders of the bank, who subscribed their receipts from the bank shares (1,125,000 livres in bills of state and 375,000 livres in specie) for the stock of the new company. Law found it necessary, in order to stimulate the sale of the shares, to buy publicly some two hundred shares at par, of which 200 livres per share was paid as a margin, with the option of completing the transaction in six months. Dealing in options (*marché à prime*) was thus brought into general practice for the first time in France. The making of the contracts for the tobacco monopoly, the extension of the commercial operations of the company and the wresting of the farming of the revenues from the Paris brothers, who had formerly controlled it, gave a great stimulus to the market value of the stock, and Law was authorized to issue fifty thousand new shares at a premium of one hundred per cent., to pay the government the sum guaranteed by the new contracts. The value of the old shares was maintained by requiring their presentation to obtain the new ones. The original issue thus came to be known as the "mothers" (*mères*) of the second, which were called the "daughters" (*filles*), while the third issue was known as the "granddaughters" (*petites-filles*). The contract with the government for assuming the entire public debt upon a pledge by the state to pay annually three per cent. interest was authorized October 12, 1719, and the payment of the interest was assured to the company by its contract for collecting the revenues. Three successive issues of one hundred thousand shares in the *Compagnie des Indes*[1] were thought necessary to carry through this gigantic operation. The new shares were of a par value of 500 livres each but were issued at a price of

[1] The name of the *Compagnie d'Occident* was changed to the *Compagnie des Indes* in May, 1719, when the privileges of the two companies of the West Indies and of China were absorbed by Law's Company, and the new name was retained until the dissolution of the company in 1769.—Courtois, 20.

5000 livres, payable ten per cent. a month. The presentation of the old shares was not required for the purchase of these last issues and the price was rapidly forced upward until 10,000 livres per share was attained in November, 1719.

Whatever might have been the success of so comprehensive a scheme under sound management, the fever of speculation had forced the shares to a point where a reasonable dividend was impossible. Law announced at a general meeting of the shareholders on December 30, 1719, a total revenue of 91,000,000 livres,—48,000,000 from the interest on the public debt, to be retained from the taxes; 12,000,000 from profit on the farming of the taxes; 6,000,000 from tobacco; 1,000,000 from general taxes not covered by the farming of the revenues; 12,000,000 from profits of the coinage; and 12,000,000 from the commercial operations of the company. The actual par value of the outstanding shares was 312,000,000 livres, which would have afforded a profit of nearly thirty per cent., and a dividend of 200 livres per share was actually declared on January 1, 1720; but the shares had been selling at 12,000 livres, or twenty-four times their par value, which afforded an actual dividend of only one and two-thirds per cent. Notwithstanding the doubtful character of some of the profits claimed and their palpable insufficiency to pay large dividends upon such an inflated investment, the phrenzy of speculation forced the shares by January 6, to 18,000 livres—thirty-six times their nominal par value. The Rue Quincampoix, between the Rue Saint-Denis and the Rue Saint-Martin, had been since the close of the reign of Louis XIV. the meeting place of speculators and dealers in the public stocks. Such operations attained a new extension by the speculations in the shares of the *Compagnie des Indes*. Fortunes were won and lost in a day and feeling became so violent that the place was closed by the government and the speculators were driven into obscure corners in other parts of the city, where they were constantly on the watch for the police.[1]

[1] The decree of October 25, 1720, forbidding speculative operations in the public streets is of interest because it established the sixty

The New Year of 1720 and the declaration of the dividend marked the apogee of Law's system. The craze had substantially run its course and the reaction was setting in. Prices were rising under the impulse of the excessive issues of bank-bills and the more prudent speculators were endeavoring to convert their gains into more solid property by the purchase of real estate or by shipping gold abroad. The bank had already been authorized to issue 1,000,000,000 livres and there had been issues without authority and counterfeits, which were easily made because the genuine bills were so rapidly and crudely turned out. Specie began to disappear and the subsidence of speculation made the bills redundant. Law adopted the now familiar argument in favor of paper money, that it was to be preferred over coin because it was non-exportable. A series of decrees during the early months of 1720 sought to discredit coined money and maintain the currency of the bank-bills. The nominal value of coin was reduced; the quantity of specie which an individual was permitted to hold was limited; the sale of vessels of gold or silver was prohibited; the carrying of diamonds and precious stones was prohibited; the circulation of bills throughout the realm as legal tender was decreed; an advantage was accorded those who paid certain taxes in bills rather than specie; and special jurisdiction was given the Council of State for causes concerning bank-bills.[1] All these measures failed to maintain confidence in the super-

agents of exchange (*agents de change*) who still form the legal body of the Paris Bourse. Their places are transmissible and hereditary. The Bourse decides what stocks shall be admitted to its lists and only those representing a large capital are ever listed. The corporation which has been formed by the members inspires absolute confidence in its operations by voluntarily assuming corporate responsibility for the acts of its members in their legitimate capacity as brokers. This corporation has instituted a clearing house and was strong enough in the crisis of 1882 to borrow 80,000,000 francs ($16,000,000) from the Bank of France, guaranteed by the Rothschilds to the amount of 40,000,000 francs and by the leading societies of credit for 40,000,000 more.—Jannet, 347–48.

[1] Courtois, 44.

abundant mass of paper and the control of the bank was turned over to the *Compagnie des Indes*. The company was authorized to convert at the will of the holders shares in the company into bank-bills or to redeem bills in shares, at a fixed price of 9000 livres per share. The contest of paper money against the metals was continued by a decree of March 11th, suppressing gold and silver as legal tender and providing for the confiscation of gold or silver, whether coin, bullion, or vessels, when found in the possession of subjects.

But the tide had turned and could no longer be stemmed. The fall in the stock continued, the company suffered in its commercial operations by the pest, which closed the free port of Marseilles, and a decree of May 1, 1720, scaled the value of shares from month to month until they should be reduced on December 1st, to 5500 livres and bank-bills should be reduced to fifty per cent. of their par value. Panic seized upon every holder of either form of paper, as he saw the values of his property shrinking under legal decree with every passing day. A commission was appointed to examine the bank and found that against 3,000,000,000 livres of circulation it held 21,000,000 livres in coin, 28,000,000 in bullion and 240,000,000 in commercial bills,—less than ten per cent. of assets in all against its outstanding notes. A run upon the bank began on the night of July 16th, and the crowd was so dense that a dozen unfortunates were choked or trampled under foot. The corpses were placed upon litters and borne to the residence of the Regent. Law escaped from the crowd into the palace, but his carriage was broken in pieces and the coachman thrown from his seat and dragged upon the ground. The bank was closed, the forced legal tender of the bank-bills was suspended, the contracts of the company with the government were cancelled, and the stock was called in for readjustment.

A decree appeared on January 26, 1721, known under the name of the *visa*, providing for the liquidation of the affairs of the company and of the bank and the readjustment of the public debt. The decree was attributed to Paris-Duverney, from whom Law had taken the farming of the revenues, and

was confided to him for execution. The attempt was made to readjust private fortunes as well as public obligations upon the basis which had prevailed before the period of paper inflation which Law had inaugurated. Those who had fled the country with their winnings transmuted into gold, those who could command the royal favor, and those who were able to keep their gains in hiding were the only ones who escaped. The mere transfer of speculative gains into real property did not prevent the exercise of arbitrary power to transfer the property back to its original owners and remit the new owner to his original poverty. A regular scale of readjustment was prepared by which the public debt was reduced to its original volume and the holders of bills and the stock of the company were given new public obligations ranging from one hundred per cent. of their holdings in certain cases down to five per cent., according as they were supposed to represent real values or the profits of stock gambling.

The lesson of Law's disastrous schemes and the painful readjustment which followed them prevented for half a century the creation of any new bank of issue in France. The success of the Bank of England, however, and the necessity of some aid to commerce, led to a futile attempt to found a bank under a decree of the Council of State of January 1, 1767,[1] and the establishment, during the ministry of Turgot, by a decree of March 24, 1776, of the *Caisse d'Escompte du Commerce* (The Bank of Commercial Discount). The new institution was limited to a strictly banking business, and forbidden to borrow except by its notes payable at sight. It was authorized to begin operations with a capital of 15,000,000 livres ($3,000,000), of which it was intended that two-thirds should be loaned to the Treasury. The loan to the Treasury not having been completed as proposed, the capital of the bank was reduced to 12,000,000 livres, repre-

[1] The proposed institution was to be known as the *Caisse d'Escompte* and to have a capital of 60,000,000 livres, but it never entered upon active operations and was suppressed by a decree of March 21, 1769. —Courtois, 84.

sented by four thousand shares of 3000 livres each. Some of the most eminent public men and financiers of Paris served on the board of directors of the bank, and while they were not directly responsible for its management,[1] its note issues were kept within prudent limits and annual dividends were declared for the first six years, ranging from five to eight per cent.

The first blow to the bank's credit came from the demands of the government. The growing social and economic difficulties of France were brought to a climax by the bad crops of 1783 and caused a great scarcity of metallic money. The new bank, after having considerably expanded its commercial discounts, made an advance to the government at the demand of D'Ormesson, of 6,000,000 livres. It was brought face to face with the crisis with a circulation of 45,000,000 livres and with a cash reserve of but little more than 4,000,000. There was a sudden rush for the redemption of the notes and the bank appealed to the Treasury to reimburse the 6,000,000 livres recently loaned. The government was in no condition to comply with this demand, but it was ready to employ its sovereign power to enable the bank to suspend specie payments and to authorize the redemption of bills in commercial paper or their non-payment until January 1, 1784, (Decree of September 27, 1783). The bank was solvent, however, and had the courageous support of the private bankers of Paris, who held a large proportion of its bills. A report presented by the lieutenant of police, M. Le Noir, showed that the bills in circulation, amounting to 44,724,000 livres, were offset by 47,700,000 livres in good commercial paper, 4,121,700 livres in gold and silver coin and bullion, and 6,000,000 livres held by the Treasury,

[1] The bank really constituted a partnership *en commandite*, for which a few individuals were legally responsible, and the use of the names of leading financiers as directors was somewhat akin to the modern fraud of paying men of high station for the use of their names to float irresponsible enterprises; but the practice in this case appears to have grown out of the lack of experience with stock companies and to have involved no intentional deception.

making total assets of 57,821,700 livres and affording a favorable balance of 13,097,700 livres.[1]

The loan to the government was soon repaid, specie payments were resumed under a decree of November 23, 1783, and the bank was authorized to increase its capital to 15,000,000 livres, and for four years it continued to operate free from government interference and with advantage to the business community. Its growing prosperity attracted the attention of Calonne, then Controller General, and he determined to turn it to account for the benefit of the State by requiring the deposit of a guarantee fund with the Treasury. The capital was raised from 15,000,000 to 100,000,000 livres and the net receipts in cash, amounting to 80,000,000 livres, were deposited to the amount of 70,000,000 with the Treasury and 10,000,000 were carried to the reserve. A new run set in in August, 1787, but the directors refused to accept a decree for the suspension of specie payments, which Loménie de Brienne, Chief of the Royal Council of Finance, was preparing, demanded help from the guarantee fund in the possession of the government, and promptly met every obligation.

But the government was sinking into the sloughs of bankruptcy and determined to drag the bank with it, so that there should be no stronger credit than its own to put it to shame. August 18, 1788, appeared a decree authorizing the bank to redeem its bills in part in commercial paper. The decree was unsought and its existence was unknown until it was affixed to the doors of the bank, and the permission to suspend was not embraced by the directors. But Necker, who became Finance Minister on May 25, 1789, continued to insist upon secret loans to the Treasury, and the government and the bank soon became so involved with each other that Necker proposed to transform it into a national bank. The Constituent Assembly had already assumed the power to regulate the bank, as it regulated all the established institutions of France, and ordered it to pay into the Treasury 80,000,000 livres of its bills against a deposit of interest-bearing *assignats*. The bank lost its credit with the business commu-

[1] Noel, I. 90.

nity, the redemption of its notes in *assignats* was decreed in 1790, bank-note issues were forbidden by the law of August 17, 1792, and the institution was suppressed by a decree of the National Convention on August 24, 1793.

The next three years were those of the consummation of the Reign of Terror, the execution of the King and Queen, the fall of Danton and Robespierre, and the restoration of order under the Directory. "What institution of credit," asks M. Horn, "could have braved the tempest which agitated the end of the eighteenth century? What instrument of credit could have maintained itself against the *assignats*, which destroyed alike the notions of value and of money?"[1] But the Saturnalia of fiat money lasted but little longer than in the time of Law. The same sort of enactments,—making the paper money legal tender for debts at its nominal value, fixing maximum prices, punishing those who discredited the assignats in conversation,[2] and inflicting the penalty of death upon those who kept their produce from the market,—quickly ran their course. The *assignats* in circulation amounted on January 1, 1796, to 27,565,237,396 francs, and had increased on September 7, to 45,578,810,040 francs, when they were worth one one-thousandth part of their nominal value. The whole fabric disappeared at a blow when the National Assembly decreed on July 16, 1796, that every one might transact business in whatever money he chose and that the mandates, which had superseded the *assignats*, should be taken only at their current value. The effect of this removal of the restrictions upon the natural laws of money is thus strikingly portrayed by Professor MacLeod:

> No sooner was this great blow struck at the paper currency, of making it pass at its current value, than specie immediately reappeared in circulation. Immense hoards came forth from their hiding places; goods and commodities of all sorts being very cheap from the anxiety of their owners to possess money, caused immense sums to be imported from foreign countries. The exchanges immediately turned

[1] *La Liberté des Banques*, 317.

[2] Courtois, 99.

in favor of France, and in a short time a metallic currency was permanently restored. And during all the terrific wars of Napoleon the metallic standard was always maintained at its full value.[1]

The end of the paper money phrensy saw credit again raising her head and several new banking institutions under way. The first one, founded in 1796, was known as the *Caisse des Comptes Courants* (Bank of Current Accounts), and had a capital of 5,000,000 francs ($1,000,000). The circulation was 20,000,000 francs in bills of 500 and 1000 francs, and bills of exchange running for ninety days were discounted at six per cent.[2] The *Caisse des Comptes Courants* was created largely by bankers for bankers, and a party of business men, to escape what they regarded as a certain degree of favoritism, determined to found a banking association of their own. They established, November 24, 1797, for a term of three years, the *Caisse d' Escompte du Commerce* (Bank of Commercial Discounts), which proved so successful that it was renewed for an unlimited term. There was no fixed capital, but each new subscriber for a share of 10,000 francs ($2000) increased the capital by so much until in less than four years it had reached 12,000,000 francs. Five thousand francs were paid on each share in cash and five thousand francs in bank-bills were endorsed by the subscriber with his own signature and afterwards countersigned by the bank.[3] The plan proved so successful that it was imitated by the retailers, who organized the *Comptoir Commercial* (Commercial Bank). The *Caisse des Comptes Courants* and the *Caisse d' Escompte* accepted reciprocally each others bills and were doing an active and safe banking business when a new turn was given to the economic history of France by the *coup d'état* of the Eighteenth Brumaire (November 9, 1799), which made Napoleon Bonaparte First Consul and virtually the supreme ruler of France.

Bonaparte had hardly grasped power before he turned to his financial advisers for a plan for a national bank. They

[1] *Theory and Practice of Banking*, II., 258.

[2] Courtois, 109.

[3] Horn, 322.

had one ready for his immediate consideration, bearing a striking resemblance to the plan of the Notary Rouen which had been before the Council of Five Hundred under the government of the Directory. Less than three months after the Eighteenth Brumaire appeared the decree of January 18, 1800 (*28 Nivose, An VIII*), constituting the Bank of France, with a capital of 30,000,000 francs in shares of 1000 francs each. The decree provided that one-sixth of the capital should be furnished by the Treasury by an investment of half the funds given as bonds by the receivers general, and Napoleon, members of his family, and personal friends lent their support by subscribing for the shares.[1] This support was necessary to the success of the bank, and it was not until 1802 that all the shares were taken. Vitality was given the institution by the decision of the general assembly of the *Caisse des Comptes Courants* to consolidate with it and the transfer of their offices in the Place des Victoires. February 20, 1800, the bank began its operations as a bank of issue and of discount. It was at the outset a private institution, free from government interference and its right to issue notes was far from exclusive.

But Bonaparte did not view with patience this situation. "One bank is easier to watch than several," was his comment, and after the *Caisse d'Escompte du Commerce* had refused to loan money to the government, he took vigorous measures to drive it to the wall. The law of April 14, 1803 (*24 Germinal, An XI*), gave the Bank of France the exclusive privilege of issuing bank-bills at Paris, raised the capital from 30,000,000 to 45,000,000 francs and decreed that no bank should be established in the departments without the authority of the government. The stockholders of the *Caisse d'Escompte du Commerce* filed an emphatic protest against the abrogation of their right to issue notes. Their complaints did not prevent the passage of the law, but the

[1] Napoleon took thirty shares, Joseph Bonaparte took one share, Murat two, Hortense Beauharnais ten, Duroc five, General Clark, who married Napoleon's sister and died in San Domingo, one, and Bourienne, five.—Noel, I., 97, note.

management of the Bank of France did what they could to prevent a crisis by fusion with existing banks of issue. A consolidation was arranged with the *Caisse d'Escompte du Commerce*, which turned over its assets and received bills of the Bank of France in exchange. The shareholders had the option of becoming shareholders of the Bank of France with all the privileges of the original shareholders.

The financial crisis which broke out upon the formation of the third coalition against France, after the rupture of the Peace of Amiens, resulted in radical changes in the constitution of the Bank of France. The preparations for the campaign of Austerlitz required large expenditures by the government and the syndicate of contractors for supplies for the armies obtained large loans from the bank in the form of bills. The bills began to be presented for redemption at the rate of two or three million francs a week. The coin reserve of the bank was reduced, specie was demanded by the bank in the settlement of its balances with bankers in the departments, and accommodation bills of exchange were largely drawn by the contractors to obtain new loans, with the result of new note issues and new demands for redemption. The circulation, which before 1803 had never exceeded 30,000,000 francs, surpassed 80,000,000 and the bills began to fall below par. The council of the regency limited redemptions to a fixed sum per day, and in course of time the contraction of discounts and the settlement of balances due the bank reestablished equilibrium. The victory of Austerlitz (December 2, 1805) assisted in restoring confidence, and Napoleon, the morning after his return to Paris, summoned a council to discuss the crisis which had absorbed his thoughts even upon the field of battle.[1]

The Emperor was convinced that bad management had much to do with the crisis, and within twenty-four hours of the council M. Mollien succeeded M. de Barbé-Marbois as Minister of the Treasury and was charged with the preparation of a new plan of organization for the bank. He recommended that the bank be linked with the State and that it

[1] Noel, I., 104.

be the only institution in the country authorized to issue credit paper. "The bank," he declared, "does not belong only to its stockholders; it belongs also to the State, since the latter has given it the privilege of creating money." This policy was very pleasing to the Emperor and was promptly put in practice. The law of April 22, 1806, increased the capital of the bank from 45,000,000 to 90,000,000 francs and confided its direction to a governor and two subgovernors named by the head of the State, but paid by the bank. The duration of the privileges of the bank was extended fifteen years beyond the date fixed by the Act of 1803, until September 24, 1843. It was the purpose of Napoleon to make the bank national in its operations as well as in name, and a decree of May 18, 1808, gave the exclusive privilege of note issues to the bank in every town in which it established branches.

The fall of Napoleon caused a temporary suspension of the operations of the bank. The council ordered the burning of the bills which were in the vaults ready for issue and the withdrawal of current accounts by depositors. The reserves fell to 5,000,000 francs ($1,000,000) the circulation to 10,000,000 francs and current accounts to 1,300,000 francs. The prompt return of peace restored confidence, the circulation was increased to 70,000,000 francs and the reserves rose to 93,000,000 francs. The government of the restoration, however, was not especially friendly to the financial creation of the Napoleonic dynasty. The management of the bank themselves were ready to renounce exclusive privileges in the departments, provided the stockholders were allowed to resume the selection of the governor and his assistants. This project was not accepted by the Chambers, but the branches at Rouen and Lyon were abandoned and were succeeded by departmental banks of a type which soon spread to the leading cities of France.

These departmental banks were entirely independent of the Bank of France, and were authorized to issue their own notes. They accommodated themselves to local necessities, their officers were acquainted with local credits, their profits

augmented, and their operation contributed greatly to the development of the industrial activity of the nineteenth century in France. Institutions of this sort were founded in nine principal cities, and some idea of the extent of their operations and of their success may be formed from the following table of the principal items of their balance sheets for 1847 :[1]

BANK.	MEAN COIN RESERVE.	MEAN DISCOUNTS.	MEAN CIRCULATION.	DIVIDENDS.
	Francs.	Francs.	Francs.	Per Cent.
Rouen,	4,500,000	10,100,000	12,000,000	14.4
Nantes,	1,700,000	6,400,000	4,300,000	9.7
Bordeaux,	12,600,000	13,900,000	20,900,000	16.3
Lyon,	10,400,000	23,100,000	19,700,000	28.8
Marseilles,	6,400,000	14,000,000	16,500,000	12.9
Havre,	1,600,000	7,000,000	4,400,000	6.8
Lille,	1,800,000	5,400,000	4,500,000	9.6
Toulouse,	1,600,000	2,400,000	4,800,000	11.7
Orléans,	1,100,000	2,600,000	3,000,000	11.3
Total,	41,700,000	84,900,000	90,100,000	

This exhibit shows a circulation for these nine banks in 1847 of about $17,500,000 secured by a coin reserve of $8,000,000, by means of which loans had been made to the amount of $18,000,000. The large profits obtained by these departmental banks (indicated in the table of dividends) were reflected in the high prices of their capital stock. The shares all had a par value of 1000 francs ($200), and the quotations in 1847 were: Bank of Rouen, 2650 francs; Nantes, 1750 fr.; Bordeaux, 2200 fr.; Lyon, 3770 fr.; Marseilles, 1970 fr.; Havre, 1330 fr.; Lille, 1700 fr.; Toulouse, 1200 fr.; Orléans, 1810 fr. The deposits were comparatively small, amounting at their maximum in 1847 to 16,800,000 francs ($3,250,000). Deposit banking was almost unknown in the smaller cities of France and these departmental banks

[1] This table is compiled from the appendix to Courtois's *Histoire des Banques en France*, 338–41, and is given in round figures because the tables appear there in millions of francs, instead of being fully carried out. The same figures appear in Horn's *La Liberté des Banques*, 361–64.

could never have made substantial dividends or acquired any considerable volume of business without the power to transmute their assets into circulating notes.

The majority of the departmental banks were founded between 1835 and 1840,—the period when the failure of the Bank of France to meet expanding commercial needs began to be most keenly felt. The Bank of France was generally regarded as an institution for bankers rather than for merchants and the latter obtained their discounts at the bank through the intervention of private discount houses. Many of these houses suspended during the political disturbances of 1830, and it became necessary to appoint a royal commission to report upon the commercial and industrial situation and "to propose measures suitable to restore to business transactions and the circulation their usual regularity." The proposition which became law on October 17, 1830, proposed to make loans directly from the Treasury and fixed the amount at 30,000,000 francs ($6,000,000). A discount office (*Comptoir d'Escompte*) was established at Paris with a capital of 1,300,000 francs, which it was authorized to lend at four per cent. on bills upon Paris and at five per cent. on those upon the provinces. Various amounts were afterwards added to the capital and the *comptoir* was continued with the guarantee of the City of Paris until September 30, 1832. The total discounts from December 31, 1830, covered 59,928 pieces of commercial paper amounting to 33,191,433 francs. Similar offices were established in many of the departments and contributed with the direct government loans towards the accommodation of industry. The government commission made loans in Paris for periods of twelve, eighteen, and twenty-four months, distributing them with some reference to the number of laborers employed, and assisted nearly 450 establishments in fifty-three departments outside of Paris, employing more than eighty thousand men.[1] The amount of these loans reported still bad or doubtful in 1870 was 905,312 francs ($180,000).

A similar device was resorted to again after the revolution

[1] Courtois, 137–45.

of 1848. The country was then emerging from the effects of a financial crisis and the discount houses had again lost public confidence. The government on this occasion sought the co-operation of the business community in establishing discount offices. They required that a third of the capital be furnished by individuals or municipalities, the other two thirds being represented by Treasury bonds and municipal obligations. Some of the offices received in addition a loan in specie, upon which they were required to pay four per cent. interest to the Treasury. Most of these loans were reimbursed at the end of two years and several of the discount offices afterwards repaid the capital advanced by the State and became private banks. The Paris office became the *Comptoir d'Escompte*, which established branches in India, Japan, and the Antilles,[1] and carried on some large operations in finance. It was wrecked by advances of 130,000,000 francs to the great copper syndicate in 1888, and its ruin was proclaimed by the suicide of the director, M. Denfert-Rochereau, on March 5, 1889.[2] The Bank of France was compelled from 1848 to 1852 to make many renewals of its discounts, but the amount thus outstanding was reduced on December 31, 1856, to 772,500 francs ($150,000).[3]

The success of the departmental banks was already so great before 1840 that the Bank of France was stimulated to avail itself again of the right to establish branches in the leading cities of the country and a contest which has not yet ended arose among bankers and economists as to the relative wisdom of granting a monopoly of note issues to a single institution or permitting such issues by local banks. The advocates of monopoly won a partial triumph by the Act of June 30, 1840, which prolonged the privileges of the Bank of France until December 31, 1867, and declared that no departmental bank should thenceforth be established, nor the privileges of existing banks prolonged, except by virtue of a special law. The ordinance of March 25, 1841, which

[1] Courcelle-Seneuil, 194.
[2] Jannet, 325–26.
[3] Courtois, 178–187.

fixed the status of the branches, is the law still in force, and gave to the branches the exclusive privilege of issuing notes in the cities where they were established. Even the increase in the number of the departmental banks and in the branches of the Bank of France had not been adequate to supply the growing demand for discounts, and in 1837 Jacques Laffitte founded the *Caisse Générale du Commerce et de l'Industrie* (General Bank of Commerce and Industry),[1] with a capital of 15,000,000 francs. The absence of authority to issue circulating notes was evaded by the issue of bills payable to order after five, fifteen, and thirty days, with interest, and for three months without interest. The bills payable after five days were the most sought for and were circulated with an indorsement in blank which permitted them to pass from hand to hand.

The overthrow of the government of Louis Philippe in February, 1848, came on the heels of the financial crisis of 1847, and the combination of the two events caused a long list of failures and the general suspension of specie payments by authority of the provisional government. The suspension of specie payments was accompanied by decrees giving forced legal tender character to bank-notes, both those issued by the Bank of France and those issued by departmental banks,[2] but legal tender circulation was given the notes of the departmental banks only within the departments

[1] The Bank of France was unwilling that the name *Banque* should be assumed by any other institutions than itself and the departmental banks. There was no law on the subject, as in England and the United States, but the object was attained by the suggestion that cordial relations would not be established with the new institution if it called itself a bank.—Courtois, 155, note.

[2] The opponents of monopoly lay stress upon the fact that the Bank of France was forced first to seek the suspension of specie payments, and it was not until ten days later (March 25, 1848) that the same privilege was extended to the departmental banks, which had thus far steadily met all demands. The circulation of the Bank of France was fixed by legal decree at a maximum of 350,000,000 francs ($70,000,000) and limits were fixed for each of the departmental banks, amounting to an aggregrate of 102,000,000 francs ($20,400,000).—Horn, 368–70.

in which they were established. This policy, whether intentionally or not, paralyzed the action of the independent banks and gave a color of justification for the decrees of April 27 and May 2, 1848, providing for the fusion of the departmental banks with the Bank of France and limiting the issue of bills to the central institution and its branches. The language of the decree based the consolidation upon the ground "that the bills of the departmental banks form in certain localities special monetary signs, whose existence injects a deplorable perturbation into all transactions; and that the essential interests of the country imperiously demand that every bank-bill declared to be legal money shall be able to circulate equally in all parts of the land." [1] The government thus touched upon the weakest feature of the departmental system—the lack of interchangeability of the various note issues. This was in part the result of the government's own action in limiting the legal tender quality of the notes, but it was also true that there was no association among the banks which might have kept their notes in circulation without the legal tender quality. [2] The Bank of France was given the aggregate circulation of the pre-existing banks and the maximum was raised by decree of December 22, 1849, to 525,000,000 francs.

The fusion of the departmental banks with the Bank of France resulted in an increase of the capital of the central institution by the exact amount of the capital of the nine departmental banks. The capital of the central bank had been reduced in 1823 by the purchase of outstanding shares to 67,900,000 francs and was increased by the absorption of the departmental banks to 91,250,000 francs ($18,000,000). So strongly did the current of centralization run that it was proposed to unite the bank to the public domain under the name of the National Bank of France, but the Assembly was unwilling to increase the distrust already felt in business circles by so radical a departure and rejected the proposals. [3]

[1] *Lois et Statuts*, 67–68.
[2] Courtois, 175–6.
[3] Noel, I., 114.

The forced legal tender of the bills came to an end by the law of August 6, 1850. A new increase of capital was made by the law of the Empire of June 9, 1857, and the charter of the bank was extended to December 31, 1897. Its existing privileges were confirmed and a concession was made to the recent growth of economic opinion, in favor of controlling the foreign exchanges through the discount rate, by exempting the bank from the usury laws.[1] The new charter required that branches be established within ten years in all the departments, but it was not until fifteen years after the time set that this requirement was fully complied with. The increase of capital was justified by the immense expansion of industry by machinery and the building of railroads, and the requirement of a branch in every department made it the more imperative. The capital was therefore doubled and the 91,250 new shares were issued at 1100 francs, of which the premium of 100 francs was destined to strengthen the reserve. The government borrowed 100,000,000 francs of the money subscribed for the increase of capital upon a pledge of three per cent. securities.

The strength of the bank proved a powerful support for the railway enterprises which were now being floated in nearly every department. The quotation of the stock of the new companies, which had not yet had time to complete their lines, had fallen very low when ten of the leading companies formed a syndicate and appealed to the bank for assistance. A contract was signed by which the bank opened a credit in favor of the companies on the deposit of their obligations and agreed to market them under favorable conditions. Two hundred and forty million of francs ($46,300,000) of obligations were disposed of, 150,000,000 by private sales and 90,000,000 by public subscription, during 1858, and the quotations were carried upward from 260 francs to 290 francs within the year. The only benefit derived by the bank from this operation was the interest on the advances

[1] *Lois et Statuts*, 81. The earnings above six per cent. were required to be carried to a permanent surplus fund, which has stood for more than twenty years at 8,002,313 francs.

to the companies, which amounted to 449,600 francs, but the operation was so successful that sales through the agency of the bank were continued in 1859 and the bank charged a commission of 50 centimes for each obligation sold, deriving a premium of 440,000 francs from the transaction. Similar operations were continued for several years, with handsome profits to the bank and great benefit to the railways in placing their obligations and obtaining the necessary capital for construction.

The history of the Bank of France since 1870 is deeply colored by the national struggle with Germany. The bank lent its support to the government at the outset; it received the privilege of legal tender for its notes and the suspension of specie payments; it suffered from the ravages of the Commune, and it played a large part in the settlement of the great war indemnity. The management of the bank was prudent, and its credit suffered but slight impairment under the strain of national disaster and civil discord. The bank advanced 50,000,000 francs to the government on July 18, 1870, four days after hostilities were voted, secured by Treasury bonds running for three months. Other advances up to the close of the war carried the total to 1,470,000,000 francs ($280,000,000). The suspension of specie payments was authorized on August 12th, with only one dissenting vote in the Chamber of Deputies. This step was not taken at the request of the bank, or because of any severe pressure upon it for gold, but with the view of tying up the gold reserve for the benefit of the government in case of military necessity.[1]

The restoration of specie payments in 1850 had been accompanied by the removal of any limitation upon note issues, which had gradually expanded with increasing commercial development to 1,439,000,000 francs ($275,000,000) in 1869. A limit of 1,800,000,000 francs was imposed by the law of August 12, 1870, which was raised two days latter to 2,400,000,000 francs. Gold jumped to a premium of fifteen per cent., but the premium fell in a few days to

[1] Courtois, 258.

one per cent. or even less and did not rise materially, in spite of the disasters of the army, until the great demand for foreign exchange in paying the war indemnity. The premium then rose as high as twenty-five per cent., representing apparently one of the few cases where the price of gold has risen as the result of a special demand without affecting the prices of commodities or the credit of the paper circulation. The necessity of a large circulating medium led to a further extension of the limit of issue on December 29, 1871, to 2,800,000,000 francs, and the great loan of three milliards was the occasion for another extension, July 15, 1872, to 3,200,000,000 francs. The law of December 29, 1871, authorized the issue of notes for five francs and ten francs. The limit of circulation was not again raised until after the resumption of specie payments. Resumption was set by the law of August 3, 1875, for the time when the debt of the government to the bank should be reduced to 300,000,000 francs. This condition was formally complied with by a payment to the bank of 10,000,000 francs on December 31, 1877, but the bank had already been paying five-franc pieces in silver since November 7, 1873, and twenty-franc gold pieces since November, 1874.[1]

The Bank of France was saved from complete destruction during the reign of the Commune in Paris, in the spring of 1871, by appeasing with small sums the appetites of the hungry Communist leaders. The latter first drew out in instalments the sum of 9,401,819 francs, which was on deposit to the credit of the City of Paris, and when this was exhausted demanded several millions more. The bank yielded grudgingly under the compulsion of force and with the approval of the Ministry of Finance at Versailles. The Communists, after the capture of one of the gates of Paris by the regular army on May 22d, set fire to the Tuileries and sent one of their officers to the bank to demand the immediate payment of 700,000 francs for the wages of the National Guard. The Marquis de Plœuc, the Assistant Governor, temporized as far as possible by advancing 200,000 francs

[1] Arnauné, 349.

and refusing the remainder upon the ground that so large an advance required the consent of the Council of Regents of the bank. The refusal exasperated the Communist leaders, who threatened to bring the bank to terms by two battalions and two pieces of cannon. The bank yielded, upon the written demand of the Committee of Public Safety, endorsed by M. Jourde, the financial delegate of the Commune, that "If this sum is not delivered, the bank will be immediately invaded by the Communal Guard."[1] M. Jourde was obliging enough, when a new demand was made for 500,000 francs on May 23d, to deliver a receipt endorsed with the declaration that "The refusal of this sum would involve the seizure of the bank." The next day the regular army of Versailles was in the heart of Paris and the bank was safe from further robbery. The advances on behalf of the City of Paris were recognized as a debt of the city and counted into the loan for 210,000,000 francs contracted with the bank on August 30, 1871. The bank was less successful with the general government and, after a long course of negotiations, was obliged to charge 7,293,383 francs to the account of profit and loss.[2]

The Bank of France played an important part in the most remarkable transaction in the history of foreign exchange—the payment of the great war indemnity levied upon France by Germany. A detailed account of the process of payment was submitted to the National Assembly in 1875 by M. Léon Say, and forms one of the most instructive chapters of modern financial history. The definitive treaty of peace, signed at Frankfort on May 10, 1871, called for the payment by France to Germany of five milliards of francs ($1,000,000,000). Five hundred millions were to be paid thirty days after the restoration of order in Paris, one thousand millions during the year 1871, five hundred millions on May 1, 1872, and three thousand millions on March 2, 1874, with five per cent. interest on the last payment. The framers of the treaty appreciated the difficulty of making such an immense

[1] Noel, I., 122.
[2] Noel, I., 200.

transfer of credit without upsetting the financial fabric of Europe and provision was made that payment might be made in gold or silver, in notes of the banks of England, Prussia, Holland, or Belgium, or in first class bills of exchange. Bills not payable in Germany were to be valued at their net proceeds after deducting the cost of collection. It was afterwards agreed that the portion of the Eastern Railway of France which was situated in the ceded province of Alsace, and was the property of the French government, should be accepted for 325,000,000 francs of the indemnity, and that 125,000,000 francs should be received in notes of the Bank of France.

Three things had to be accomplished in order to pay the indemnity within the time set. The credits had to be transferred to the French government by taxation or the sale of securities; the proceeds had to be converted into obligations acceptable to the German government; and these obligations had to be paid or transferred to the credit of Germany. The first step was taken by means of an advance from the Bank of France and the placing of public loans. The bank advanced 1,530,000,000 francs ($300,000,000) to enable the government to meet promptly the two payments required during 1871. One of the conditions of the payment of the indemnity was that German troops should occupy French soil until the payments were completed. M. Thiers, the president of the new republic, determined to free the country from foreign occupation at the earliest possible moment by anticipating the payments. Two loans were authorized, —one for 2,225,994,045 francs ($430,000,000) in the summer of 1871, and one of 3,498,744,639 francs ($675,000,000) in the summer of 1872. They were subscribed many times over and the government thereby obtained the funds for completing the payments and liberating French soil in the summer of 1873.

One of the striking results of this loan was to bring from the hoards of the French peasants and small shop-keepers the gold and silver which had been accumulating for generations. It was the initiation of whole classes of the French

people into dealing with negotiable securities. The time was nearly ripe in the progress of modern financiering for this change in the habits of the people, but it required a loan which appealed to their patriotism and carried a high guarantee of safety to definitely break down the old habit of hoarding and establish the new habit of investment.[1] The subscriptions to the second loan were 934,276, and the amount subscribed was 13,252,455,930 francs at Paris, 4,513,445,566 francs in the provinces, and 26,050,195,054 francs in foreign countries. The foreign subscriptions, numbering 107,612, were largely speculative and the majority were made by the great financial houses as a means of supporting their correspondents in Paris. The bulk of the loan tended eventually into the hands of Frenchmen. The hoards of gold and silver brought into the market from the provincial subscribers went to swell the monetary circulation and enabled the Bank of France within a few years to accumulate a coin reserve nearly twice as large as it had ever before held. While 375,000,000 francs ($73,000,000) in gold left the country in the three years 1871–73 and the reserve of the Bank of France declined as low in 1871 as 399,000,000 francs, the yellow metal came pouring back in the next few years, and in 1876 the reserve of gold alone in the bank stood at 1,530,400,000 francs ($300,000,000).

Another striking feature of the payment of the war indemnity was the development of the use of commercial credit for transferring funds from one country to another.

[1] M. Leroy-Beaulieu computes an increase in French fund-holders from 550,000 in 1870 to 1,000,000 in 1876, counting only permanent investors and excluding speculative holdings. This would represent about one in eight of the heads of families in France. The sales of public securities in the departments increased from 4,299,425 in 1869 to 24,272,094 in 1873.—*La Science des Finances*, II., 220–25. The effect of the popular subscriptions may be traced also in the reduction of the balances in the *Caisse d'Épargne* (Savings Bank) of Paris, which fell from 54,180,747 francs ($10,500,000) on January 1, 1870, to 35,454,124 francs ($7,000,000)on January 1, 1873, the latter being the lowest point reached since 1850.—*Vide Bulletin de Statistique*, Oct., 1895, XXXVIII., 374–77.

The aggregate payments consisted of only 742,334,079 francs ($143,000,000) in all forms of currency, including bank-notes, and 4,248,326,374 francs ($820,000,000) in bills of exchange. The loss in the monetary circulation of France was less than the sum of coin and bank-notes, because some of the bank-notes were purchased by exchange in foreign countries and others were German notes which had drifted into France with the German army. The real specie payments were 273,003,058 francs ($52,600,000) in French gold and 239,291,875 francs ($46,000,000) in French silver. The essential work of completing the payments was done by the purchase by the government of bills of exchange drawn by Frenchmen upon their credits in every quarter of the world. British bills were the most plentiful upon the Paris market and the heavy purchases of the French government threw much of the monetary stress upon England and compelled the Bank of England to maintain high discount rates all through 1872 and 1873.[1] The purchase by the government of a bill drawn by a French merchant upon an English customer permitted the transmission of the bill to the German government, which could then draw upon London for the gold or simply direct the deposit of the proceeds to their credit in the London Joint Stock Bank, which was their London agent. If the Frenchman who sold his bill of exchange to the government was a purchaser of the new public loan, the result of the process was the transformation of his claim against his English customer into a claim against his own government.

One of the incidents of this great operation in exchange was the fall in the price of foreign securities on the Paris market and their flight to other countries, where their quotations remained comparatively undisturbed. These influences operated most directly upon what are known on the European exchanges as "international securities," because they are known and quoted in the leading markets of the world. The cause of their decline on the Paris market in 1871 was the eagerness of Frenchmen to transfer their capi-

[1] Gilbart, II., 384.

tal into the obligations of their own country. The result of the decline was not only the sale of the securities offered to brokers, but a flood of foreign money and foreign credits to Paris to take advantage of the reduced prices of "the internationals." M. Say, in his report, attributed to these arbitrage transactions in international stocks and their coupons much of the facility with which the indemnity was paid. The sales of Italian five per cent. securities alone on the Paris Bourse from July 1, 1871, to December 31, 1873, were 46,115,000 francs ($9,000,000), not including sales by private brokers. The proof that these sales were largely on foreign account was furnished by the decline in the interest payments made at Paris on Italian securities from 40,150,000 francs on July 1,1871, to 25,604,000 francs on January 1, 1874.[1]

The Bank of France was embarrassed as early as 1860 by the fluctuations in the relative value of gold and silver and their departure from the ratio of fifteen and a half to one fixed by the French coinage law of 1803. Silver had become the more valuable metal, because of the immense addition to the gold stock by the discoveries in California and Australia. The value of silver, in other words, was greater in proportion to gold than the price paid for bullion at the mint. It was obvious that if the bank continued the policy of redemption of its notes in gold or silver at the option of the holder, silver coin would always be preferred, and would be withdrawn for speculative purposes as long as it could be obtained, because it could be sold as bullion at a profit above its face value in gold. The situation became so serious that the bank asserted the option to pay only in gold and was obliged to borrow that metal from the Bank of England in order to be well supplied. Gold had been flowing into France since the opening of the California mines and silver

[1] Leroy-Beaulieu, II., 236. M. Leroy-Beaulieu admits that sales for *report* are included in the first item, but the decline in interest payments at Paris seems to sustain his argument that Italian securities left France in order that their proceeds might be invested in the indemnity loan.

flowing out in an uninterrupted stream,[1] but the Bank of France had held on to the dearer metal, silver, and redeemed in the cheaper until its gold reserve was reduced in 1860 to about 100,000,000 francs, while its silver stood at about 325,000,000 francs. About £2,000,000 in gold was obtained from the Bank of England, which was not averse to exchanging the less valuable metal for the dearer, even though the latter was not a money metal in England.

The departure of the market ratio of gold and silver from the mint ratio by the depreciation of gold was the occasion of the formation of the Latin Union. Belgium, Italy, and Switzerland had already adopted the French decimal system of coinage before the formation of the Union, and the coins of each country circulated freely in the others. The proposition for a conference came from Belgium, but was cordially accepted by the French government and the meeting called at Paris. The most pressing problem to be confronted was the disappearance of the subsidiary silver coins because of the premium upon silver. Switzerland had already reduced her silver coins, except the five-franc piece, by the law of January 31, 1860, from nine-tenths fine to eight-tenths; Italy, by the law of August 24, 1862, had lowered to 0.835 fine the franc and smaller pieces; and France had adopted the standard of 0.835 for her pieces of 20 and 50 centimes. The change of all but the five-franc piece was recommended by a commission appointed by the French government in 1861, but the Corps Legislatif in passing the law of May 25, 1864, refused to reduce the one- and two-franc pieces.[2] Belgium was on the point of taking legislative action when the advantages of an international conference suggested themselves.

The refusal of the French legislative body to reduce the fineness of the larger silver pieces, so as to bring their bullion

[1] The net imports of gold into France from 1848 to 1870 were 5,153,000,000 francs ($1,000,000,000) and only one year (1861) showed net exports. The years 1852 to 1864 showed uninterrupted net exports of silver amounting to 1,726,000,000 francs ($340,000,000).—Shaw, 184–86.

[2] Arnauné, 191.

value down to their face value, was rapidly driving them out of circulation and silver had long ceased to be offered in any considerable quantities for coinage at the mints.[1] The conference decided that all silver coins below the five-franc piece should be reduced to 0.835 fine, that their coinage should be limited in each country to six francs per capita, that the subsidiary silver should be received in the public depositaries of each country in amounts not exceeding one hundred francs ($19.30) and should be a legal tender in the country where coined in amounts of not more than fifty francs ($9.65). The Belgian, Swiss, and Italian delegates strongly urged the adoption of the single gold standard, but the proposition was resisted by the French delegates and was not acted upon. The convention putting in effect the decisions reached in the conference was adopted on December 23, 1865, and Greece soon after became a party to it. A monetary conference was held at Paris in connection with the international exposition, which recommended the adoption of the gold standard by the countries taking part, and it was in pursuance of this action that the French government concluded the preliminary convention of July 31, 1867, with Austria, establishing a fixed relation between the franc and the gold florin.[2]

The formation of the Latin Union, so generally treated today as a plan to maintain bimetallism, was, in the language of a high authority, "a measure of defence against the action of the bimetallic system in those countries which had adopted the monetary system of France, and lay exposed to all its disastrous fluctuations."[3] The effect of the action of the countries forming the Union, in the language of the French monetary commission of 1867, "places in the front rank gold money, and reduces the pieces of silver of two francs and less to the rôle of token money. It therefore

[1] The total coinage of silver at the French mint in 1863 was 329,610 francs ($65,000), while the gold coinage was 210,230,640 francs ($41,000,000). The largest silver coinage since 1856 had been 8,663,568 francs in 1858, and the largest gold coinage 702,697,790 francs in 1859.

[2] *Vide* Ch. viii. and ix.

[3] Shaw, 190

definitely determines the ascendency of the gold franc and solves practical difficulties arising from the double standard." The Latin Union, so far from establishing bimetallism, adopted the gold franc as the standard because gold was then the money of general circulation within the countries of the Union. The mints continued open to the free coinage of both metals, but silver was not offered on private account for coinage into five-franc pieces at the legal ratio, any more than gold would be offered at the present day in a country where silver at the old ratio was the common medium of circulation.

It was because the ratio tilted backwards to a higher bullion value for gold and a declining value for silver that the aspect of the monetary problem was reversed and that the purpose of the Latin Union has come to be misunderstood. The members of the union from the outset, however, have done no more than seek to maintain the circulation of silver by limiting its coinage. Silver first dropped below par in 1867, when the commercial ratio of gold to silver was 1 to 15.57, but it was not until 1873, when the quotation was 1 to 15.92,[1] that it began to be noticed that an excessive quantity of silver was being minted and that gold was disappearing from circulation. The problem was complicated by the fact that France, Italy, and Greece were under the *régime* of paper money, leaving only Belgium and Switzerland in full enjoyment of the bimetallic coinage system. The latter

[1] The statement of these differences in the terms of the ratio makes them look much more trifling than is really the case. Stated in terms of percentage, the depreciation of silver in 1867 was a little less than one-half of one per cent. (0.45) and in 1873 was 2.7 per cent. of the par value. The depreciation in 1872 was 0.97 per cent. It is interesting to note that the changes prior to 1873 took place, and that their effect was visible in the bullion offerings at the mints, before the adoption of the gold standard in Germany or the United States or the limitation of coinage by the Latin Union. The depreciation of nearly one per cent. in 1872 was sufficient to afford a large profit on bullion operations, in view of the fact that the usual element in such computations—the time consumed in earning interest—did not need to be considered.

country, with a keen appreciation of actual conditions, almost entirely suspended silver coinage and received her circulation from the other countries of the union.[1] The presentation of gold for coinage at the French mints ceased during 1872 and 1873, and the silver coinage was 26,838,369 francs in the former and 156,270,160 francs in the latter year. The mint of Belgium was besieged by the owners of silver bullion and 111,000,000 francs in five-franc pieces were coined in 1873, while even Italy, though on a paper basis, coined 42,000,000 lires, which were refused acceptance by the Bank of France.[2]

The limitation of the coinage was resorted to for the four years ending with 1877 as the only means of averting the single silver standard. Conferences were held annually and the maximum coinage of five-franc pieces was fixed for each country. The aggregate of these allowances for the four years was 45,200,000 francs for Belgium, 216,000,000 francs for France, 18,000,000 francs for Greece, 164,000,000 francs for Italy, and 28,800,000 francs for Switzerland. Italy was allowed to coin 29,000,000 francs in 1878 and 1879, on condition that the sum should be retained in the Bank of Italy as a metallic reserve against the circulating paper money. Silver continued to fall in price and the policy of limitation was succeeded in 1878 by the policy of absolute suspension of the coinage of five-franc pieces. The monetary union was renewed from 1878 to January 1, 1886, and was extended in 1885 to January 1, 1891, since when it has been prolonged annually by mutual agreement. The convention of 1885 not only bound each of the contracting parties not to resume the coinage of five-franc pieces without the consent of the union, but provided that if such coinage should be resumed the coins should be redeemable by the nation coining them in gold on demand, and that if such

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[1] Her entire coinage of five-franc pieces, from the first limitation to the final suspension of silver coinage, was only 7,978,000 francs ($1,500,000).—Haupt, 85–86.

[2] Arnauné, 197.

redemption should be refused the coins might be refused by the public depositaries of the other parties to the union.'

It was such conditions which confronted the Bank of France when it prepared to resume specie payments in 1877 with a gold reserve of 1,202,400,000 francs ($232,000,000) and a silver reserve of 860,900,000 francs ($165,000,000). The situation was exactly the same as in 1860, except that the position of the two metals was reversed. The bank found itself well stocked with the more valuable metal, but restrained from using it for redemption purposes because of the certainty that it would soon be drawn away and sold as bullion. The policy was adopted, and has been steadily adhered to, of redeeming in gold or silver at the discretion of the bank and charging a premium for gold. It is impossible to obtain gold at the bank in the quantity desired for exportation and it has to be taken from the domestic circulation. This means of protecting its gold reserve has been treated by the bank in some measure as a substitute for raising the rate of discount in a monetary pressure and while it protects the gold of the bank it has none of the advantages upon the money market which follow the different policy of the Bank of England. The bullion shippers were shrewd enough when discount was low and gold at a premium in 1857, to draw gold by discounting accommodation bills at the bank rate of four per cent. and selling the gold for the premium for exportation. The bank prevents this under its present practice by paying for discounted paper in silver, which is not exportable for monetary purposes. The result,—"to defend the reserve of the bank to the detriment of the reserve of the country," in the language of M. Arnauné—"is an error which may have melancholy consequences."[2]

The excessive quantity of silver in the reserve of the bank has contributed in a measure to its large note circulation. The bank has tried to force silver five-franc pieces into cir-

[1] For the arrangements regarding the liquidation in gold of the excess of foreign silver coins in France, see Chapter xi., under the Bank of Belgium.

[2] *La Monnaie, le Crédit, et le Change*, 397.

culation, but they have drifted as steadily back upon its hands as standard silver dollars, in spite of the efforts of Treasurer Jordan, drifted back into the Treasury of the United States in 1885 and 1886. People have preferred to take notes resting upon the security of both the gold and silver in the bank reserves. The bank, in the language of an eminent Scotch financier, has had to "relieve the public of £50,000,000 of silver, which was coined, and was in excess of the silver required for the purposes of the people."[1] The government proposed the removal of the limit on circulation in 1884 and while this was refused, the maximum was carried up by the law of January 30, 1884, from 3,200,000,000 francs to 3,500,000,000 francs. The actual circulation at this time was 3,162,000,000 francs, but it continued to rise in response to the demand of the public for notes. The excess of notes in circulation over gold and silver was 1,210,000 francs in 1884 and was reduced in 1893 to 695,000,000 francs, while the circulation had climbed upwards on January 12, 1893, to 3,473,000,000 francs. Another extension of the legal limit was demanded for the accommodation of commerce and it was carried upward by the law of January 25, 1893, to 4,000,000,000 francs.[2]

The fluctuations in the gold and silver holdings of the Bank of France are in some degree an epitome of its history. Gold was scarcely a factor during the years before the discovery of the Californian and Australian mines, but after 1852 it rapidly expelled silver from the vaults until the bank took measures to reserve what was then the more valuable metal. The swing of the ratio backward in favor of gold in 1867 was followed by accumulations of silver which have not driven out the gold because of the option which the bank has exercised to pay in either metal. The figures for representative years, in francs, are as follows:

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[1] Mr. Charles Gairdner, manager of the Union Bank of Scotland, before the Indian Currency Committee. Sen. Misc. Doc. 23, 53d Cong., 1st Sess., 150.

[2] Arnauné, 326-27.

YEAR.	GOLD.		SILVER.	
	Maximum	Minimum	Maximum	Minimum
1811	21,714,000	18,301,000	105,231,000	91,228,000
1820	51,817,000	22,488,000	167,372,000	136,925,000
1830	1,700,000		171,800,000	102,500,000
1840	26,700,000	10,000,000	235,000,000	185,600,000
1850	29,200,000	5,500,000	339,100,000	290,700,000
1852	86,800,000	63,900,000	447,000,000	349,700,000
1855	171,000,000	28,300,000	92,400,000	25,000,000
1857	95,900,000	36,500,000	35,400,000	25,300,000
1860	238,300,000	97,400,000	325,100,000	269,000,000
1865	391,200,000	215,900,000	142,800,000	93,900,000
1868	877,100,000	662,400,000	477,300,000	308,800,000
1870	739,300,000	433,700,000	579,600,000	70,900,000
1875	1,176,100,000	1,004,300,000	508,700,000	309,200,000
1877	1,556,500,000	1,204,100,000	866,700,000	637,100,000
1880	826,900,000	536,400,000	1,282,500,000	1,212,000,000
1885	1,175,800,000	995,300,000	1,106,100,000	1,024,400,000
1890	1,320,900,000	1,114,200,000	1,276,900,000	1,239,100,000
1892	1,708,300,000	1,336,200,000	1,299,000,000	1,248,500,000
1893	1,720,900,000	1,537,200,000	1,285,500,000	1,247,900,000
1894	2,061,500,000	1,695,500,000	1,283,100,000	1,237,400,000

The most important functions of the Bank of France relate to the monetary circulation. The volume of commercial discounts has, however, grown to considerable proportions of late years and has included the rediscounting of very minute pieces of commercial paper presented by the discount banks of Paris. The number of pieces discounted by the central bank in 1894 was 5,805,774, and of these 2,188,957 pieces were for 100 francs ($20) or less, and more than half of these were below 50 francs. The number of pieces of 100 francs or less in 1881 was 1,160,495, and in 1885 1,590,839. The bank has suffered in the volume of its discounts from the competition of banking companies of more compact organization and with fewer public responsibilities, which have kept their discount rates more closely in harmony with those of the money market. The rate of discount at the bank[1]

[1] M. Neymarck suggests that the bank should, upon the renewal of its charter, be authorized to lend at less than the official rate on the best paper, as is done by the Bank of England. By adhering uniformly to the official rate, he argues, the bank drives the first-class paper (*papier de choix*) to other lenders and gets only that of inferior quality.—*Du Renouvellement du Privilege*, 10-11.

was for many years kept at four per cent., in defiance of the rates in other countries and outside the bank, and even at present is less often changed than in other large banks. The rate fixed on May 19, 1892,—two and a half per cent. for commercial discounts and three and a half per cent. for advances on securities—remained for nearly three years unchanged, and was only reduced to two and three per cent. on March 14, 1895. This was still the rate at the beginning of 1896.

The fact that the bank's most important functions relate to the circulation may be deduced from the figures of its transactions. The circulation exceeds by more than three times the discounts and advances, and the metallic reserve is many times the entire liability on account of deposits. The circulation on January 2, 1896, was 3,647,097,410 francs. The commercial discounts at Paris were 346,394,931 francs and at the branches 503,356,005 francs. The advances on securities at Paris were 182,603,486 francs and at the branches 201,936,317 francs. Discounts have fallen off somewhat during the past two years, because the bank rate has been higher than that of London and of other money lenders, but the commercial discounts at the central bank and branches were only 681,000,000 francs on January 4, 1894, and reached the temporary elevation of 983,000,000 francs on April 26th, only because of the negotiation of an important loan by the City of Paris.[1] If discounts are relatively small, deposits are still smaller, and if they are of minor importance at Paris, they are insignificant at the branches. The deposits at Paris on January 2, 1896, were 562,259,304 francs ($107,000,000) and at all the branches 90,041,157 francs ($17,000,000). The discounts given in the following table of the principal items of the bank's accounts, from the official reports to the government, represent the aggregate of the bills discounted during the year rather than the amount outstanding on any given date :

[1] Raffalovich, *Le Marché Financier en 1894–95*, 23.

YEAR.	MEAN CIRCULATION.	MEAN METALLIC RESERVE.	TOTAL DISCOUNTS.	MEAN DISCOUNT RATE.
	(In millions of francs)			
1845	268.8	271.2	1,399.3	4.00
1848	347.8	176.2	1,537.4	4.00
1850	495.5	457.8	1,171.0	4.00
1855	644.4	340.5	3,765.2	4.44
1860	736.4	513.5	9,964.7	3.63
1865	843.8	439.6	6,030.2	3.72
1870	1,566.4	1,130.7	6,627.3	3.99
1875	2,464.9	1,541.1	6,826.7	4.00
1880	2,311.4	1,974.4	8,696.8	2.81
1885	2,891.6	2,150.7	9,250.1	3.00
1890	3,076.6	2,476.7	9,549.7	3.00
1892	3,186.3	2,785.3	8,415.7	2.50
1893	3,423.0	2,895.3	8,922.2	2.50
1894	3,495.0	3,127.7	8,725.6	2.50
1895 [1]	3,484.9	3,202.9	———	2.00

The Bank of France enjoys the advantage of an ownership and credit independent of that of the government, in spite of the close official supervision which is exercised over it. This financial independence proved as useful to the country midst national disasters and changes of government in 1870–71 as dependence upon the government proved dangerous during the similar changes of 1814–15. The bank was able to assist the government by advances when its own arms were paralyzed.[2] None of the 182,500,000 francs of the bank capital are owned by the State, but the government since 1806 has had a share in the management through the appointment of the governor and two deputy governors, removable at the will of the Minister of Finance. The bank receives the public monies on deposit and performs other public services free of charge, but does not act as an agent of the State to the same extent as many other European banks. The Treasury is entitled to an advance of 140,000,000 francs ($28,000,000) and receives the proceeds of a stamp duty on the notes and a tax of four per cent. on dividends. The proceeds of these taxes in 1894 were about 2,500,000

[1] Actual condition, December 26th.

[2] Noel, I., 240. M. Thiers summed up one of the lessons of sound banking in a sentence: "The bank saved us because it was not a bank of state."

francs ($500,000). There is no division of profits with the government, but this has been repeatedly proposed in connection with re-charter. The requirement that the bank shall maintain a branch in each department has now been complied with, and ninety-four branches, thirty-eight auxiliary bureaus, and 116 other banking offices are in operation. Each branch is under the charge of a director appointed by the government upon the nomination of the governor of the bank.

The governing board of the bank is a general council, which consists of fifteen regents and three inspectors or auditors (*censeurs*). The members are elected at a general meeting of the stockholders, but three of the regents must be selected from the treasury disbursing agents, and three inspectors and five regents must be chosen from among the business portion of the shareholders.[1] The only shareholders entitled to participate in the annual meetings in January are the two hundred who hold the largest number of shares, and at the present value of the shares no shareholder worth much less than 500,000 francs ($100,000) is able to participate.[2] A full statement of operations is furnished by the bank to the government every six months and a balance sheet is published in the official journal every Friday. The expenses of the central bank for 1894 were 7,464,600 francs and of the branches 6,521,100 francs. Transportation and other general expenses of 2,447,822 francs raised the total to 16,433,522 francs ($3,200,000). Fifteen branches showed an excess of cost over net earnings in 1894 amounting to 156,831 francs ($31,000). The number of employees of the

[1] *Lois et Statuts*, Art. 9, loi du 22 Avril, 1806.

[2] Neymarck, 15. This provision has been the subject of much criticism in connection with the renewal of the charter and it has been pointed out that the bank is the only one of the great European institutions where the number entitled to vote in the general meetings of the shareholders is thus difinitely limited. A minimum number of shares is the usual qualification, being only one in the Imperial Bank of Germany, five in Holland and Servia, ten in Belgium, fifteen in Italy, twenty in Austria-Hungary, and fifty in Spain.—Noel, I., 222.

central bank in 1894 was 1074 and of the branches 1258. The dividends distributed in 1894 were 117.7 francs per share, including the impost of 4.7 francs. The highest dividend paid was 350 francs in 1873. This was 35 per cent. of the par value of the shares, but only 8.09 per cent. on the market value, which was about 4370 francs. The value of the shares on December 31, 1894, was 3600 francs.

The Bank of France may be confronted in the immediate future with a struggle for existence. The renewal of the charter was proposed in 1891, but the opposition was so strong in the Chambers that the bill for the purpose was withdrawn by the ministry for fear of defeat. Two potent influences are arrayed against the renewal of the monopoly of note issues by the bank under the terms of the existing charter. On one side stand the classical political economists, who believe in the theory of free banking and point to the success of the departmental banks before 1848 and the development of the Scotch and American systems, in support of the policy of diffusing agencies of credit and of note issue throughout the country. On the other side stand the socialists, who believe that the bank should be turned into a great machine for scattering paper riches among the people in the form of pensions and insurance, in payment for public works, and in the purchase of the instruments of transportation and communication by the State. The close of the year 1897 will witness the expiration of the charter, unless legislation is enacted in the meantime to extend it. It is possible that the government will exercise the executive power of prolonging the charter for a year or two, as has already been done in the case of some of the colonial banks whose charters expired in 1894.

CHAPTER IV.

FIRST CENTURY OF THE BANK OF ENGLAND.

The Economic and Financial Conditions Out of Which the Bank Grew—Early Difficulties and the First Suspension of Specie Payments—The Loans of the Napoleonic Wars and the Restriction of 1797—Pitt's Enormous Drafts upon the Bank.

THE Bank of England, like many of the Continental banks, had its origin in the needs of the State. The institution which resulted has been several times the victim of the monetary necessities of the government, but has not been dragged quite so persistently as the banks of Italy, Austria, and Russia through the mire of depreciated money and forced legal tender. The Bank of England has come to enjoy, by a series of changes in the law, the substantial monopoly of note issue in England and Wales, and has proved one of the strongest banking institutions of the world. The note circulation, since the Act of 1844, is based wholly upon securities and deposits of coin and bullion. The rigidity of the English system, by which expansion is prevented to meet changing conditions of business, has received the condemnation of most students of political economy, but this has not kept it from becoming to some extent the model of national banks of later foundation on the Continent of Europe. The defects of the English system of note issues are those which are most apparent in a country where deposit banking is in its infancy. They are less obvious and oppressive in England than they would otherwise be because of her small area, the wide use of credit instruments and the closely-knit commercial relations of her people.

The creation of the Bank of England is involved with both the political and fiscal history of the close of the seventeenth century. England was behind Italy and Holland in the development of the mechanism of modern commerce, and the proposition to establish a banking system was sharply resisted by Gerard Malynes, who published in 1601 a *Treatise of the Canker of England's Commonwealth*. Malynes described the Continental method of banking with a fairness and precision which enable its leading features to be readily understood, in spite of his opinion that payments by the banks by transfers upon their books were "almost or rather altogether imaginative or figurative."[1] English merchants deposited their cash for a time in London Tower, but £120,000 was seized by Charles I., in 1640, and only repaid after violent protests and long delay.[2] The goldsmiths then became the bankers for the community and paid interest for the money left in their custody. There was much opposition to the new system at first and, strange to say, one of the last to adhere to the old method of keeping his cash in a strong box at home was Sir Dudley North, one of the most progressive thinkers on political economy of his time. As Macaulay graphically recounts North's experience, "He found that he could not go on Change without being followed around the piazza by goldsmiths, who, with low bows, begged to have the honor of serving him. He lost his temper when his friends asked where he kept his cash. 'Where should I keep it,' he asked, 'but in my own house?'"[3]

While commerce was coming to feel more and more the need of a banking institution, the government was also feeling the necessity of some method of raising money beyond the precarious plan of sending agents to individual merchants to see what they would lend. The historic legend that King James I. attempted out of a spirit of pure wantonness to levy excessive and unusual taxes upon the people of

[1] Cunningham, II., 98.
[2] MacLeod, *Theory and Practice of Banking*, I., 435.
[3] *History of England*, Chap. xx.

England is not fully borne out by the facts. The method of taxation which he sought to introduce was simply a phase of the transition from feudal to modern methods of carrying on public affairs. As a careful student of the economic history of England puts it :

> According to ancient usage the King had been able to live of his own, and had recourse to Parliament in emergencies. The chief problem of the seventeenth century was to find a source of revenue which would supply a regular income, that might adequately correspond to the increased responsibilities of government in these more modern times. The first attempt to do this was in the Great Contract, proposed to the Parliament in 1610 ; by this James proposed to relinquish all the occasional payments from feudal tenures, in return for a regular income of £200,000 to be derived from parliamentary supplies.
>
> As this bargain broke down, James was a considerable sufferer ; Charles I., to whom Tunnage and Poundage were not voted for life, was left in a position of direct dependence on parliamentary grants, and he did not conceal his resentment. During both of these reigns every effort was made to secure supplies from extra-parliamentary sources ; while the Commons, who were eagerly anxious to assert their position and exercise a real control over the foreign as well as the domestic policy of the realm, were always on the alert to thwart these attempts. [1]

The parliamentary party succeeded in organizing a system of taxation by means of customs duties, monthly levies upon real estate and excises on internal trade, which continued in full force after the restoration of the Stuarts. These taxes laid the foundation of the modern method of defraying the expenses of government, but they were inadequate for many extra expenses and for carrying on the wars in which Charles II. and William III. found themselves involved. Charles II. turned for assistance to the goldsmiths. But his rapacity soon outran his borrowing capacity, and he gave a violent shock to credit by a proclamation of January 2, 1672, refusing payment out of the Exchequer of money advanced and sequestrating £1,328,526 to his own use. The money, although lent by the goldsmiths to the King, was the prop-

[1] Cunningham, II., 215.

erty of some 10,000 depositors and its loss spread ruin and suffering throughout London. A long course of litigation ensued, which finally ended in the reign of William by the consolidation of the indebtedness with other portions of the permanent national debt.[1] This conduct on the part of the Stuart King made the people and the bankers cautious about loaning to the government, and William III. was driven to desperate expedients to obtain revenue to carry on the war with France. A poll tax was imposed, stamp duties were levied which have never been entirely repealed, and enormous prizes, in the form of annuities on the tontine plan, were offered to those who would lend to the State.

A plan was presented to the Committee of the House of Commons, while they were considering the claims of the goldsmiths in the autumn of 1691, which contained the germs of the organization of the Bank of England. William Paterson, himself an obscure Scotchman, but supported by several wealthy London merchants, offered to advance £1,000,000 to the government on condition of receiving £65,000 a year as interest and the costs of management and authority to issue bills which should be legal tender. The government refused to give forced currency to the bills and the matter fell through until 1694. Montague, the ingenious and enterprising minister of William, then sent for Paterson and requested him to organize a plan. The new project contemplated a loan of £2,000,000 to the government at seven per cent., but the ministry, who were accustomed to discounts and commissions of forty per cent. on short loans, could not be made to believe that a loan with no fixed date of maturity could be floated at such a low rate. The government turned to other plans, but Paterson persevered and presently obtained the help of Mr. Michael Godfrey, who carried the scheme to a successful conclusion. It was put in definite shape by Montague and was saddled upon the Ways and Means bill (Statutes 1694, ch. 20), in a form which would be characterized in modern legislation as "a rider."

[1] MacLeod, *Theory and Practice of Banking*, I., 441–44.

"The Governor and Company of the Bank of England" was the official designation of the new bank, but it was called by its enemies the Tonnage Bank, because the bill levied certain tonnage dues as well as customs and other taxes. The necessity of money was so great that the bill passed without a division in the Commons, and in a very thin house. There was some opposition in the House of Lords, and much criticism of the action of the Commons in attaching the provisions for the bank to a tax bill. It was already May, according to the new style, when the final struggle occurred, and the debate of the last day continued from nine in the morning till six in the evening. It was proposed to strike out all the clauses relating to the bank, but its defenders suggested that this would be to invite a contest with the Commons over the old political issue, whether the Lords had the right to amend a money bill. This argument prevailed, the amendment was rejected, thirty-one votes in its favor to forty-three in the negative, and a few hours later the bill[1] received the royal assent and Parliament was prorogued.

The new bank was to be organized upon the loan by the stockholders of £1,200,000 ($6,000,000)[2] to the government, and was authorized to issue notes, to deal in bullion and commercial bills and to make advances on merchandise. Subscriptions were opened on Thursday, June 21st, in the Mercer's Chapel, and one-quarter of the capital was subscribed the first day. Half was subscribed within three days, and by Monday noon, July 2d, the entire subscription was completed. Among the subscribers were Sir John Houblon, the first Governor, who was descended from a Flemish refugee;

[1] The date was April 24, 1794, old style; May 4, new style. The dates here given are from the contemporary records and are old style.

[2] The value of the English pound sterling is so generally known that I have not thought it necessary in this and the following chapter to give the equivalents in United States money for the sums named. The value of the pound sterling as reported by the Director of the Mint of the United States is $4.8665, but for the purpose of computing round figures is usually taken at $5.00.

Michael Godfrey, one of the most active organizers of the bank and the first Deputy Governor; Queen Mary; the Duke of Leeds, the Duke of Devonshire, the Earl of Portland, the Countess of Carlisle, Lord Godolphin, Lady Ann Mason, Sir Stephen Fox, and Sir John Trenchard. The new bank began the discharge of its pledges to the government by paying into the Exchequer £112,000 in bank-bills, sealed with the seal of their corporation, which bore the figure of Britannia sitting on a bank of money.[1] The business of the bank was described by Godfrey, who wrote a tract in its support, as follows:

> They lend money on mortgages and real securities at five per cent. per annum. If the titles of land were made more secure, money would be lent on land at four per cent. per annum, and in time of peace at three per cent. Foreign bills of exchange are discounted at four and a-half per cent.; inland bills and notes for debts at six per cent. They who keep their cash in the bank have the first of these discounted at three per cent., and the other at four and a-half. Money is lent on pawns of such commodities as are not perishable at five per cent., and on the Fund of the City of London Orphans at five per cent.[2]

The stock of the bank was at par on December 13, 1695, little more than a year after it began actual operation, but within the next two years it had to deal with a combination of difficulties which caused the suspension of specie payments, and required all the courage and ability of the directors to surmount. The bank was essentially a Whig institution and a representative of the commercial interests of London; and it encountered the same sort of jealous hostility from the landed interest which has prevailed in more recent times against the moneyed interests of "Wall Street" and "Lombard Street." The fate of the bank was so closely bound up with that of the Revolutionary government that it was compelled to lend its support on all occasions of emergency, or run the risk of seeing the entire debt due by the government repudiated by the restoration of the

[1] Rogers, *The First Nine Years of the Bank of England*, 3.
[2] Rogers, 20.

Stuarts. The Bank, in the forcible language of Macaulay, "Was Whig not accidentally, but necessarily. It must have instantly stopped payment if it had ceased to receive the interest on the sum which it had advanced to the government; and of that interest James would not have paid one farthing." Mr. Bagehot declares that without the aid of the bank:

> Our national debt could not have been borrowed; and if we had not been able to raise that money we should have been conquered by France and compelled to take back James II. And for many years afterwards, the existence of that debt was a main reason why the industrial classes never would think of recalling the Pretender or of upsetting the Revolution settlement: the "fundholder" is always considered in the books of that time as opposed to his "legitimate" sovereign.[1]

The political enemies of the bank were supported by the goldsmiths and other financial men whose monopoly of money lending was assailed by the new institution. The managers of the bank enjoyed from the outset three privileges which gave them an immense superiority over all competitors and enabled them to reduce the charges for banking. They received the government balances; they enjoyed alone the privilege of limited liability, by which the shareholders were liable for the debts of the bank only to the amount of their investment and not for its entire liability; and they were able to loan money in excess of their deposits by reason of the circulating notes they were allowed to issue against the government debt. The goldsmiths were able to do only the business of deposit banking, and were supposed to lend only coin, or credit for which they held coin in their vaults.[2] The goldsmiths, therefore, undoubtedly felt justified by reasons of self-preservation in lending their support to any plan which would break down their powerful rival. Such a plan was presented in the scheme of a Land Bank which was brought before Parliament by Hugh Chamberlain in 1695.

[1] *Lombard Street*, Works, V., 64.

[2] Cunningham, II., 396.

Chamberlain's scheme was to issue notes upon landed property to one hundred times the annual rental, lend the notes to the owner of the land, and in some unexplained way furnish money to the government at the same time. The absolute absurdity of calculating the money value of a piece of real estate at one hundred times the rental, when the fee simple was worth only twenty times the rental, or one-fifth as much, was demonstrated over and over again, but the opponents of the Land Bank were answered that they were "usurers," and the enemies of the Bank of England were ready to catch at any scheme which promised to promote their projects. Notwithstanding its folly the scheme was authorized by law and received the royal assent on April 27, 1796 (7 and 8 William III., c. 31). The Land Bank proposed to advance to the government £2,564,000, on which interest was to be paid at the rate of seven per cent. annually, secured by a special tax on salt. The King was authorized to appoint a body of commissioners to receive subscriptions, half of which were required to be subscribed before August 1, 1696, and the whole before January 1, 1697. Subscriptions did not materialize, however, with such rapidity as expressions of sympathy for the enterprise. The Lords of the Treasury subscribed £5000 on behalf of the King, but the other subscriptions never exceeded £2100, and it is recorded about three years later that Dr. Chamberlain, "sole contriver and manager of the Land Bank, is retired to Holland, on suspicion of debt." [1]

The immediate effect of the new legislation was to depress the price of bank shares, which fell from 107 on January 31st, to 83 on February 14th.[2] Capital was not so abundant then as now and the mere offer of a new public stock was sufficient to divert investment from the old and depress its value. It was argued even by the friends of the bank that it must be the sole institution of its kind, like the banks of Venice, Amsterdam, and Hamburg, in order to retain strength and usefulness. The experience that the stocks of an existing

[1] Rogers, 56.
[2] Rogers, 50.

company declined under the influence of competition was illustrated in a striking manner by the history of the East India Company, whose stock stood at 158 in the beginning of 1692, but sank to 38 after Montague brought forward his plan for the new or English East India Company. The close calculations which are now made regarding the earning capacity and value of stocks were little understood at that time and the unreasonable declines as well as extravagant advances which occurred are illustrated a little later by the history of the Mississippi scheme in France and the South Sea Bubble.

The bank had real financial difficulties to cope with as well as those arising from political distrust and competition. The recoinage which was ordered by the Act of 7 William III., ch. 1, to take full effect on February 1, 1697, found the bank with a large quantity of clipped coin on hand for which they were bound to pay in new pieces of full weight. The new coinage was progressing too slowly to meet demands, the smallest denomination of bank-notes was £20, and the result was a run upon the bank for cash during the week beginning May 4, 1696. The goldsmiths were charged with gathering together £30,000 in notes for the purpose of breaking the bank. The directors, knowing the purpose of the demand, refused to redeem these notes, but voted to continue their payments to their ordinary customers. Sir John Houblon, who was Lord Mayor as well as Governor of the bank, succeeded in reassuring the applicants for cash for a time, and the proprietors of the bank agreed to put off their dividend. The government failed, however, to make an expected payment of £80,000 and the bank was compelled to accept an order of the Lords of the Treasury on July 13, 1696, that no public notary should enter a protest upon any bill of the Bank of England for fourteen days. As a protest could only be effective at that time when thus entered, the effect of the order was a practical suspension of specie payments, which lasted until the autumn of 1697.

It is not surprising that the bank was unable to cope with its difficulties and that many impracticable and speculative

schemes were set on foot, for the time was essentially a period of transition. The industrial and commercial world had barely set foot upon the threshold of the wonderful development of the eighteenth and ninteenth centuries. Great Britain until the time of Elizabeth had been only a second or third rate power in Europe, overshadowed by the great Kingdoms of France and Spain, by the ancient prestige of the German Emperor, and by the power of the Pope. Her influence was raised by the defeat of the Spanish Armada, but the population of England and Wales at the Revolution of 1688 was only five and a half millions, and the supremacy in the money markets and trade of the world still belonged to the bankers and merchants of Holland and Italy. The use of bank-notes, except as mere certificates against which coin and bullion was held to the full amount, had begun only thirty years before the Revolution, and the proper management of a banking currency was almost purely a problem of abstract theory rather than of practical experience. If merchant princes and the kings of finance stood upon the threshold of an unknown world, the mass of the community but dimly viewed it from afar. They were easily deluded by extravagant hopes and easily misled by the fairy tales of the splendid riches and possibilities of the Western Continent. Least of all could the general public be expected to grasp instantly the fact, which is not accepted by great masses of people to-day, that a paper currency, in order to have a steady purchasing power, must be redeemable on demand in coin. As Mr. Cunningham acutely says, regarding the run upon the Bank of England in 1696 :

> This was a principle which men did not find it easy to recognize. They saw that the man who had wealth in any shape had credit; but they did not apparently understand that bills can only be circulated, when there is a certainty that they can be met on presentation, and that wealth, in forms which cannot be readily realized, is not a satisfactory basis for a credit circulation.[1]

The suspension of specie payments was naturally followed by a depreciation in the bank-notes. The discount on July

[1] *Growth of English Industry and Commerce*, II., 397.

28, 1696, was ten per cent. and October 10th, twenty per cent. The Bullion Report, discussing this subject in 1810, declared that "the quantity of the notes became excessive, their relative value was depreciated, and they fell to a discount of seventeen per cent." This opinion, that the note issues were excessive, is supported also by the high authority of Professor Rogers,[1] but is disproved by Professor MacLeod, in so far as excess of issues is to be interpreted as implying a larger supply of money than could be absorbed by the demands of commerce. That the issues of the bank were excessive in proportion to its coin reserve is hardly a subject for dispute, in view of the account submitted to the House of Commons on December 4, 1696, showing the amount due on notes for running cash to be £764,196, and the actual cash held £35,664, in addition to £9,636 in goldsmiths' notes. That the issues were excessive in this sense is proved by the suspension of specie payments, but that they were excessive in the sense implied by the Bullion Report is shown to be untrue by the state of exchange on Hamburg, which promptly became favorable to England upon the reform of the coinage and while bank-notes were still at a discount. The test whether issues were in excess of the necessities of trade was the state of the foreign exchanges, which were at par in coin, and the depreciation in the bank-notes was plainly due to the fact that they had ceased to be redeemable in coin on demand.[2]

The collapse of the Land Bank and the necessity for new government loans led to the legislation of February 3, 1697, to increase the capital of the Bank of England and give it wider privileges. The charter was renewed until the expiration of twelve months notice after August 1, 1710, and the bank was authorized to issue notes to the amount of the subscriptions for the new loan, provided the notes were made payable to bearer on demand. It was declared that in case of default in redemption, the notes might be paid at the

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[1] *First Nine Years of the Bank of England*, 88.

[2] McLeod, *Theory and Practice of Banking*, I., 479–484.

Exchequer out of the annuity due the bank, and a trace of the theory of the legislation of 1844 appears in the provision that all notes above the sum of £1,200,000 were to bear a distinguishing mark. The new subscriptions for the capital amounted to £1,001,171; and £200,000 in bank-notes and £800,000 in Exchequer tallies, which were both below par, were taken out of circulation. The notes previously issued had borne interest, and now rose above par, while the bank was able to issue non-interest bearing notes which circulated at par. The subscriptions to the additional stock in 1697 seem to have been made by the original shareholders and were repaid to them between 1697 and 1707 from the profits of the bank.

The government was again in serious need of money when the charter was renewed in 1708 until August 1, 1732, and the bank was authorized to double its capital of £2,201,171, and to circulate £2,500,000 in Exchequer bills. The next extension of the charter was made in 1713 (Statute I., c. 11) and continued the bank until twelve months notice to be given after August 1, 1742. The subscription lists for the new stock were opened on February 22, 1709, and the whole sum was subscribed before one o'clock. The bank under this arrangement advanced £400,000 to the government without interest and surrendered £1,500,000 in Exchequer bills to be cancelled, upon condition of receiving an annuity of £106,501. The principal of both these items was added to the permanent debt, which afterwards became the basis of the note circulation of the bank. Calls for additional capital were made upon the stockholders to the amount of £656,204 in 1709 and £501,448 in 1710. Several of the debts of the government to the bank were consolidated in 1716 and reduced from six to five per cent., and £2,000,000 in Exchequer bills were cancelled in 1718 and added to the permanent debt due the bank by the government. The settlement of the affairs of the South Sea Company in 1721 resulted in the purchase of £200,000 in annuities by the bank at twenty years' purchase, making a new addition to the permanent debt of £4,000,000. These loans increased

the permanent debt to £9,375,027, exclusive of various advances of a different character which had been repaid.

The South Sea Company was essentially a Tory institution and they proposed as early as 1717 to increase their capital from £10,000,000 to £12,000,000 for the purpose of wiping out the debt due the Bank of England and several minor obligations. The bank made counter propositions, but the real contest occurred in 1719 and 1720 over the proposition of the South Sea directors to assume the entire national debt. It was estimated at £30,981,712 and was to be consolidated into one fund, to be added to the capital of the company at five per cent. interest annually. The company proposed to pay a bonus of £3,500,000 to the government in four instalments, beginning in 1721. The bank met this remarkable proposition by an offer of its own to assume the entire debt on terms which were calculated to be about £2,000,000 more advantageous than those of their rivals. The South Sea Company obtained three days to amend their offer and increased the bonus to £7,567,500. The bank rejoined with another offer of £1,700 in bank stock for every annuity of £100 for ninety-six and ninety-nine years and the reduction of the interest on the consolidated debt after June 24, 1727, to four per cent.

The South Sea bill passed the House of Commons April 2, 1720, by a vote of 172 to 55 and passed the Lords by a vote of 83 to 17.[1] The South Sea stock was forced upward to a preposterous figure under the influence of the same fever of speculation which raged at about the same time in France over the Mississippi scheme, but capital was soon sunk in this and other unproductive enterprises and the reaction wrecked the credit of the company and came near wrecking that of the bank. The directors of the South Sea Company appealed to the bank for help, goldsmiths and private bankers began to fail, and a run upon the bank itself began, which was only staved off by payments in light sixpences and shillings and by engaging men to fill up the line, draw

[1] MacLeod, *Theory and Practice of Banking*, I., 496–99.

money and re-deposit it at another window. Fortunately the festival of Michaelmas, during which the bank was usually closed, intervened and when it was over the public alarm had subsided.

The bank had weathered severe storms, had seen two powerful rivals crushed and its own monopoly confirmed, and justly felt that it had proved its capacity to endure. Thirty-eight years after its foundation, on Thursday, August 3, 1732, the corner-stone of a new building was laid in the presence of the Governor and other officials of the bank in Threadneedle Street. The directors moved from their old quarters in Grocers' Hall on June 5, 1734, and from that day "The Old Lady of Threadneedle Street" occupied the massive building which is still consecrated to her use.[1] A statue of King William, under whom the first charter was granted, stands in the hall, with a Latin inscription which accords to him the honor of official founder of the bank.

When the time approached for a renewal of the charter in 1742, the bank advanced £1,600,000 to the government without interest by a call upon their proprietors for £840,004, which raised their capital stock to £9,800,000. The advance without interest was substantially part of a process of conversion by which the interest on the original advance to the government at the foundation of the bank and on £400,000 advanced in 1708 was reduced from six to three per cent. The bank simply continued to receive the old interest payment, but doubled the principal of the loan. The charter was extended at this time until twelve months notice after August 1, 1764. Another adjustment with the government in 1746 led to the cancellation of £986,000 of Exchequer bills, upon which the bank was to receive an

[1] The buildings have been much enlarged since and now cover the whole area between Threadneedle Street, Princes Street, Lothbury and Bartholomew Lane,—a space of more than three acres. The bank originally employed about fifty clerks, but the number is now about fifteen hundred and the pay-roll amounts to about £300,000, exclusive of £50,000 paid annually in pensions.—H. J. W. Dam, *The Bank of England*, *McClure's Magazine*, IV. 460.

annuity of four per cent., and a call upon the proprietors for ten per cent., which made the bank capital £10,780,000. The rate of interest on portions of the debt amounting to £8,486,000, which had not yet been reduced, was changed to three and a half per cent. in 1749 for the seven years beginning with Christmas, 1750, and thereafter to three per cent.[1] The charter was renewed in 1764 until twelve months notice after August 1, 1786, upon the conditions of a direct payment to the Exchequer of £110,000 and a loan for two years on Exchequer bills of £1,000,000 at three per cent. The next renewal, in 1781, carried the charter along until twelve months notice after August 1, 1812, and provided for a loan for three years of £2,000,000 at three per cent. A call upon the proprietors for £862,400 in 1782 advanced the capital of the bank to £11,642,400, at which it remained until 1816, when it was increased to £14,553,000 by adding twenty-five per cent. to the stock of each proprietor from the reserved profits or "rest."

The Bank of England at its institution enjoyed no monopoly of note issues, so that Chamberlain's plan for a Land Bank was not a violation of the privileges of the older establishment. The managers of the Bank of England endeavored to protect themselves in the legislation of 1697 and secured a provision that during the continuance of the corporation no other institution in the nature of a bank should be erected or countenanced within the Kingdom by act of Parliament by bodies exceeding six persons. This provision was calculated to prevent the formation of strong joint stock banks, and dangerous rivalry was not feared from private firms of six persons with unlimited liability. An effort to narrow the limits still more closely was made in the Act of 1709 by making it unlawful "for any body politic or corporate whatsoever, created or to be created (other than the said Governor and Company of the Bank of England), or for any other

[1] The operation of 1752, by which the balance of annuities granted in 1721 were consolidated with other three per cent. stocks, gave rise to the familiar designation, "Three per cent. consols," the latter word being a contraction of "consolidated."—Gilbart, I, 43.

persons whatsoever, united or to be united in covenants or partnership, exceeding the number of six persons, in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money on their bills or notes, payable at demand, or at any less time than six months from the borrowing thereof." This clause was repeated in 1716, when the usury laws were suspended as to the Bank of England and the directors were authorized, "at their own good liking" to borrow or take up money at any rate of interest they pleased. The conception of banking at this time involved necessarily the privilege of issuing circulating notes, and it was determined to close all loop-holes in this matter upon the renewal of the charter in 1742. It was accordingly provided (15 George II., c. 13, s. 5):

> And to prevent any doubts that may arise concerning the privilege or power given by former Acts of Parliament, to the said Governor and Company of exclusive banking, and also in regard to the erecting of any other bank or banks by Parliament, or restraining other persons from banking during the continuance of the said privilege granted to the Governor and Company of the Bank of England, as before recited, it is hereby further enacted and declared, by the authority aforesaid, that it is the true intent and meaning of the Act that no other bank shall be erected, established or allowed by Parliament, and that it shall not be lawful for any body politic or corporate whatsoever, erected or to be erected, or for any other persons whatsoever, united or to be united, in covenants or partnership, exceeding the number of six persons, in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money, on their bills or notes, payable at demand, or at any less time than six months from the borrowing thereof during the continuance of such said privilege of the said Governor and Company, who are hereby declared to be and remain a corporation with the privilege of exclusive banking, as before recited.

This limitation upon the power of other corporations did not prevent the issue of promissory notes and checks; nor did it prevent the issue of bank-notes by individuals and firms of not exceeding six persons. The opportunity which this afforded for the creation of joint stock banks of discount and deposit was not understood and availed of till

much later, but the opportunity for the issue of circulating notes by individuals and small firms was availed of. The notes of the Bank of England had little circulation outside of London and the rapid development of canal building and other enterprises during the last half of the eighteenth century created a demand for a larger credit currency. Professor MacLeod declares, in speaking of the principle of monopoly embodied in the charter of 1697, that "The frightful convulsions and collapses of public credit which have taken place during the last three-quarters of a century are chiefly due to this great wrong."[1] The effect was not felt until nearly a century later, when England began to take her place at the head of the commercial nations, but after the crisis of 1782 "multitudes of miserable shopkeepers in the country, grocers, tailors, drapers, started up like mushrooms and turned bankers, and issued their notes, inundating the country with their miserable rags." Burke said that when he came to England in 1750 there were not twelve bankers out of London; in 1793 there were nearly four hundred. The Bank of England began to issue notes for £10 and £15 as early as 1759, but the private bankers issued them for smaller amounts, and in 1775 an act was passed to prohibit notes of less than twenty shillings, and two years afterwards the limit was raised to £5.

The prohibition upon note issues was probably one of the causes which contributed to the use of checks. The notes issued by private bankers were at first written on paper for any odd sum, like promissory notes. The practice was introduced by Child and Co., in 1729, of having the notes partly printed and partly written, like a modern check. These notes continued to be issued till about 1793, when the existing system was introduced, of giving the depositor a credit for the full amount of his deposit and authorizing him to draw checks at his convenience against it.[2] The issue of

[1] *Theory and Practice of Banking*, I., 479.

[2] MacLeod, *Theory and Practice of Banking*, I., 331, 515. M. Juglar (343) says that the use of checks replaced the use of bills in 1772.

notes by private bankers was not forbidden until the Bank Act of 1844, but their use gradually diminished as the greater convenience of checks came to be understood. The Act of 1742 would probably have prohibited joint stock banks of discount and deposit, if it had been supposed that they could be carried on without the issue of notes, but note issues were then regarded as a necessary part of successful banking.

The Bank of England had to face serious financial crises in 1772, 1782, and 1792. Their policy in 1772 and 1782 was to support credit and to make advances to solvent merchants, with the result that the foreign exchanges turned in their favor and general bankruptcy was avoided. Mr. Bosanquet was Governor of the bank and he adopted the policy of contracting issues while the drain of specie was going on and expanding them when the tide turned. The crisis of 1793 was precipitated by the breaking out of war with France, and was quickly followed by the stoppage of about one hundred country banks and the serious embarrassment of many others. The directors of the bank became alarmed, refused credit to strong houses and created a great scarcity in the circulating medium by the discredit cast on the notes of the country banks. The policy of contracting issues was not justified by the state of the exchanges, for gold and silver were pouring into England from France in consequence of the issue of the *assignats*, which rapidly drove coin out of circulation, and exchange was favorable with both Amsterdam and Hamburg. The absolute refusal of the bank to lend its support to credit compelled the issue of Exchequer bills by the government, which quickly improved the situation.

The long suspension of specie payments during the wars with France was brought about by the reckless and unscrupulous course of Mr. Pitt, who dictated the entire policy of the government. The relations of the bank with the government had grown closer from year to year since 1718, when subscriptions to public loans were first received there, as affording greater convenience than the Treasury.

The bank soon after began to make advances of money in anticipation of the land and malt taxes, and upon Exchequer bills and other securities.[1] They did this in the face of the provision of the charter of 1694, that if they should advance any money to the Crown whatever, except by the special permission of Parliament, they should forfeit treble the value of all such advances. The usual limit of these temporary advances was £20,000 or £30,000 and it became a subject of complaint if the amount was increased to £50,000. The limit was stretched in the American war to £150,000 and Mr. Bosanquet in 1793 became uneasy as to the legality of such advances without authority of Parliament. The directors, therefore, applied for an act of indemnity for past advances and permission to make them in the future to a limited amount, not to exceed £100,000. Mr. Pitt readily agreed to bring in a bill for this purpose, but he quietly dropped the limitation and passed the measure in this form through Parliament. He was now armed with absolute power to draw upon the bank, unless the directors should refuse to honor his bills, and he was neither conservative nor scrupulous in the use of the power.

Mr. Pitt availed himself of the new law to scatter gold broadcast over Europe to promote the combination against France, with the result of draining the country of specie and creating unfavorable foreign exchanges. He drew heavily upon the bank and drove them into such close quarters that they passed a resolution on January 15, 1795, that the Chancellor of the Exchequer must make his financial arrangements for the year without expecting further assistance from them than advances on Treasury bills not exceeding £500,000 at any one time. Mr. Pitt promised to reduce the existing advances to that amount by payments out of the first loan which was in process of subscription, but he paid little attention to such promises. The bank was compelled by the demands of the government to expand its issues in the face of unfavorable exchanges until in February, 1795, they

[1] Gilbart, I., 36.

reached £14,000,000. The drain of gold set in strongly in September, the price of gold in bank-notes rose to £4 2*s.* per ounce (about five shillings above parity, which was £3 17*s.* 10½*d.*), and the directors of the bank were compelled to sharply restrict their discounts. They gave notice on December 31, 1795, that if the applications for discounts on any day exceeded the sum to be advanced, a *pro rata* proportion of each applicant's bills should be returned, "without regard to the respectability of the party sending in the bills or the solidity of the bills themselves."[1] Matters went from bad to worse until February 11, 1796, when the court of directors adopted the resolution :

> That it is the opinion of the Court, founded upon its experience of the effects of the late Imperial loan, that if any further loan or advance of money to the Emperor, or other foreign state, should in the present state of affairs, take place, it will in all probability prove fatal to the Bank of England.
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> The Court of Directors do therefore most earnestly deprecate the adoption of any such measure, and they solemnly protest against any responsibility for the calamitous consequences that may follow thereupon.

Mr. Pitt replied that after the repeated promises he had made he saw no occasion for the resolutions and should regard them as having been adopted in a moment of needless alarm. This did not prevent him from continuing secret remittances to the Continent, but suspension of specie payments was staved off until the next year by the restriction of accommodation to merchants and the favorable crops of 1796. The advances upon Treasury bills amounted on June 14, 1796, to £1,232,649 and Mr. Pitt demanded £800,000 more in July and a like sum in August. The bank refused the second demand but granted a request by Mr. Pitt in November for £2,750,000, on condition that the advances on Treasury bills should be paid out of this loan. "Mr. Pitt," in the terse language of Professor MacLeod, "took the money but never paid off the bills."[2]

[1] Gilbart, I., 45.

[2] *Theory and Practice of Banking*, I., 524.

The landing of a French frigate in one of the Welsh harbors and orders from the government to the farmers to drive their stock into the interior, caused a run upon the Bank of England which finally brought the long dreaded catastrophe of suspension of payment in coin. The bank had been making frantic efforts for several weeks to contract their issues and had reduced them from £10,550,830 on January 21, 1797, to £8,640,250 on February 25th, but their cash was reduced on the latter date to £1,272,000. The cabinet met the next day, which was Sunday, and issued an Order in Council, "That the directors of the Bank of England should forbear issuing any cash in payment until the sense of Parliament can be taken."[1] A meeting of merchants was held on Monday, with the Lord Mayor in the chair, which adopted a resolution similar to that adopted on the successes of the Pretender in Scotland in 1745, that "we will not refuse to receive bank-notes in payment of any sum of money to be paid us, and we will use our utmost endeavors to make all our payments in the same manner." A select committee was appointed by Parliament to inquire into the bank's affairs, and found them in a prosperous condition except for the scarcity of coin and bullion. Their assets were £17,597,280, representing a surplus of £3,826,890, exclusive of the government debt of £11,686,800, which paid three per cent. Suspension of payments was enacted until June 24th and the bank was authorized to issue notes under £5. The bank-notes were made legal tender and were to be received at par in the payment of taxes. The bank was authorized to receive special deposits in coin in exchange for notes and to repay three-fourths of the amount in coin if demanded. The restriction was prolonged on June 22d to one month after the meeting of the next session of Parliament and was again prolonged on November 30th, at the next session, until six months after the conclusion of a definitive treaty of peace.

The policy of the bank in restricting commercial discounts, though forced upon it in a measure by the demands of the

[1] Levi, 74.

government, was the cause of serious complaint in the mercantile community and led to much discussion of other methods of meeting the demand for credit. The bank refused to establish branches in the country and their charter prohibited any other strong company from doing so. The very policy of restricting their issues in the autumn of 1796, which the directors regarded as a measure of extreme precaution, intensified the demand for gold by creating a scarcity of currency which led to the withdrawal of gold by depositors. The irritation among the merchants was such that a meeting was held in London Tavern on April 2, 1796, which appointed a committee to devise a plan to restore the circulating medium, if practicable without infringing the monopoly of the bank. Mr. Walter Boyd, an eminent merchant, drew up a report on behalf of the committee, authorizing a board of twenty-five members to be named by Parliament to issue circulating promissory notes upon deposits of coin, bank-bills, and commercial paper.[1] The committee were persuaded by the Chancellor of the Exchequer to delay action and nothing ever came of their plan, but it was the opinion of Mr. Boyd that the public stocks suffered as well as commercial paper by the scarcity of currency and the necessity of forced sales of securities to obtain it. Sir William Pulteney, during the debate on the bill authorizing the suspension of cash payments, asked leave to bring in a bill for another bank if the Bank of England did not resume on June 24, 1797, as was then proposed. The proposition was defeated at the time but gained such strength within the next two years that public meetings were held and pamphlets written in its support. The bank directors became alarmed, and as government was still pressing for money, they offered £3,000,000 without interest for six years as the price of a renewal of the charter. Mr. Pitt accepted the terms and passed a bill in 1800 extending the monopoly of the bank for twenty-one years after 1812, or until 1833.

[1] MacLeod, *Theory and Practice of Banking*, I., 523.

CHAPTER V.

SECOND CENTURY OF THE BANK OF ENGLAND.

The Continued Suspension of Specie Payments—The Bullion Report and the Act of 1819—The Contest against the Monopoly of the Bank of England and the Rise of the Joint Stock Banks—The Bank Act of 1844—Theory of its Operation and its Failure to Carry Out the Theory—The Recent Accumulation of Gold in the Bank.

THE great events of the second century of the history of the Bank of England have been the resumption of cash payments, the restriction of circulation by the Bank Act of 1844, and the recent accumulation of gold in the custody of the bank. The Act of 1844 has been the turning point of almost infinite discussion of the theory and practice of banking in England, but, whatever its merits or defects, it has not destroyed the character of the Bank of England as the guardian of the cash reserve of the country, nor prevented London from becoming the centre of the exchanges of the world. Freedom from danger of invasion, the development of banking and credit beyond any point attained elsewhere, a market free to the world's commerce, and a single fixed standard of value have raised England to supremacy among commercial countries and linked the history of her financial progress in some degree with that of all other nations.

The British nation was far from her present position at the close of the Napoleonic wars. Political and military triumphs had come to her, but they had been at the expense of the crippling of her merchant marine, the increase of her

debt to $4,000,000,000, and the suspension of payments in specie. The Bank of England by prudent management kept its notes for several years at par with coin and the depreciation was at first so gradual as hardly to be noticed. One of the elements of confusion in the discussion of the effect of the restriction of specie payments was the fact that bank-notes became the sole medium of ordinary transactions. The issue of £1 notes by the bank drove the gold from circulation even before the depreciation of the paper and made metal only a subsidiary money. If an effort had been made to keep the circulation saturated with coin by continuing the prohibition upon notes below £5, the depreciation of the paper would have been quickly felt by the disappearance of gold and accurately measured by the premium upon gold. The fact that the paper was maintained at a substantial parity with gold for nearly ten years while gold disappeared from circulation, misled those who did not look to the simple and indisputable facts regarding the foreign exchanges which were stated in the celebrated Bullion Report of 1810. Silver had been rapidly disappearing from circulation for some years, because the English mint ratio gave it a less value in relation to gold than the market price. The country bankers were authorized by the restriction laws to redeem their notes in Bank of England notes in exactly the same manner as they had formerly done in specie, so that the expansion and contraction of the country note issues was in a measure placed in the hands of the central bank as well as the control of its own circulation.

Bullion rapidly accumulated in the bank after the suspension of specie payments and the bank announced their willingness on January 3, 1799, to redeem sums under £5 and to pay in full after February 1st, notes for £1 and £2, dated prior to July 1, 1798.[1] The bank then held £7,000,000 in coin and bullion and had increased its note issues to £16,000,000. The government were not willing to take the risk of resumption and continued the restriction even after the peace of Amiens,

[1] Gilbart I., 49.

when the bank again declared that it was well supplied with cash and was ready to resume. A bill was brought in on April 9, 1802, only thirteen days after the signature of the definitive treaty, to continue the restriction until March 1, 1803, and the restriction was continued again on February 28, 1803, until six weeks after the beginning of the next session of Parliament. War broke out before this date arrived and the restriction was continued until six months after the ratification of a definitive treaty of peace. No such treaty was ratified until after the abdication of Napoleon in the spring of 1814, when the problem of restriction was again taken up.

The price of gold began to rise in September, 1799, and in June, 1800, had reached £4 5*s.* per ounce, which was about seven shillings above the mint price.[1] Exchange with Hamburg fell and the unfavorable state of the exchanges was made an excuse for postponing the resumption of specie payments after the peace of Amiens. The fact that the unfavorable exchange was due to the depreciation of the currency was denied or evaded by the Parliamentary leaders and Mr. Addington, the Chancellor of the Exchequer, urged that the restriction be continued because, "for several months past, there has been a trade carried on for purchase of guineas with a view to exportation."

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[1] The mint price of gold was £3 17*s.* 10½*d.*, which was four and a half pence above the market price, in order to cover the cost of coinage and the loss of interest while the bullion was detained in the mint. The value of gold coins was fixed as they exist to-day in 1717, when it became necessary, upon the recommendation of Sir Isaac Newton, to reduce the coining value of the gold in the guinea to arrest the exportation of silver. The reduction made the ratio of gold to silver about fifteen and a quarter to one, but as the ratio in France and Holland was about fourteen and a half, it continued to be profitable to export silver from England to those countries and to import gold into England. Silver disappeared from circulation, gold became the sole metallic medium of exchange, because it was the cheaper metal at the legal ratio, and the law of 1816, which gave England the gold standard, simply recognized in law what had been the fact prior to the suspension of cash payments.

An object lesson in the effects of a depreciated currency was afforded the English people by the condition of affairs in Ireland, which had a currency of her own. The Irish shilling contained thirteen pence, and as the pound, both English and Irish, contained two hundred and forty pence, English money was more valuable than Irish in the proportion of £100 to £108 6*s.* 8*d.* The par of exchange between England and Ireland was therefore called eight and one third. The Bank of Ireland was directed to suspend specie payments at the same time as the Bank of England, and exchange was maintained at a point favorable to Ireland until the autumn after the passage of the restriction act in England. Exchange then began to fall, which made it unfavorable to Ireland, until in January, 1804, it had reached a depression of £18 in the hundred. The bank had been increasing its issues until they were more than four times the amount at the time of the restriction. A committee of Parliament was appointed in 1804 to consider the subject and they found that the exchanges were nominally unfavorable because of the depreciation of the Irish paper. The directors of the Bank of Ireland who appeared before the committee would not admit that this was the case and maintained that the large issues of paper money were to supply the place of gold which had been taken out of the country to pay remittances. One of them advanced the same extraordinary doctrine advanced a few years later in England, that "the mere buying of gold at an advanced price beyond that of the mint, is the effect, and not the cause of the exchange, and, therefore, no proof of the depreciation of the paper itself."

The committee refused to be misled by this sort of argument and found that the real exchange, when allowance was made for the depreciation in the paper, was favorable to Ireland. A convincing proof that it was so, if there were no others, was found in the fact that the exchanges between England and Belfast were favorable to Belfast, because payments at Belfast were made in specie, at the very moment that they were unfavorable at Dublin, where paper was the standard. Still further demonstration of the simple mathe-

matical proposition, that the fall in the exchange was measured by the depreciation in the paper money, and not by any cause common to Irish industry or banking, was afforded by the fact that there was a local difference of exchange between Dublin and Belfast, which put specie at a premium of ten or twelve per cent. in Dublin, while it passed at par in Belfast as the only medium of exchange.[1] The committee recommended that the relations between the currencies of the two countries be simplified by making the notes of the Bank of Ireland payable in Bank of England paper and that the Bank of Ireland establish a fund in London for that purpose. Little attention seems to have been paid to this report and the recommendation that the currencies be assimilated, which was made by Mr. Parnell in Parliament in 1809, was rejected without a division.

The depreciation of the Bank of England notes did not advance rapidly until the period of commercial speculation which caused the panic of 1810. The price of gold in bank paper, which had risen to £4 5*s*. per ounce in 1800, fell back to about £4, representing a depreciation of two and a half shillings or about three and two-tenths per cent., and remained at substantially this figure until 1809. The price of gold rapidly advanced during the following year until the mint price of gold was £4 11*s*. or a depreciation of 17.4 per cent. Exchange with Hamburg had been falling with the depreciation of the currency and on February 1, 1810, Mr. Horner moved for several accounts relating to the currency and exchanges. The committee was then appointed whose work has become so famous in the literature of finance as the Bullion Report. The committee, in an endeavor to ascertain the true cause of the unfavorable exchanges, examined a large number of witnesses, including directors of the Bank of England, private bankers, business men, and students of finance. The conclusions of the committee, however, were directly adverse to the opinions of the bankers and in accordance with those of the most enlightened students of the abstract problems of finance and political economy.

[1] MacLeod, *Theory and Practice of Banking*, II., 14.

The report which the committee presented to the House of Commons took its place at once among the classics of finance and has been one of the guides of sound banking from that time to this. It is a remarkable fact that Mr. Horner was a young man of thirty-two who had never given more than a general attention to financial subjects. He simply listened attentively to the testimony of the best experts who appeared before the committee and with singular clearness of vision grasped the correct principles of regulating a banking currency and discarded the shallow sophistries and "practical rules" which were presented to him by the great bankers of London.[1] The Bullion Report is remarkable not only for the clearness and precision with which it lays down the fundamental rules for regulating the volume of a paper currency, but for the discriminating judgment with which it discusses limitations of the then existing theories of prices and currency which only came to be generally accepted by political economists a generation later and have not been accepted by all of them to-day.[2]

The undisputed facts upon which the bullion committee based their report are summed up by Professor MacLeod as follows[3]:

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[1] M. Juglar remarks that, "There is always something which blinds those the best placed to see, and it is not the persons engaged in affairs who are the best judges of the mechanism they direct or which, rather, sweeps them along."—*Des Crises Commerciales*, 341. For similar views see Price, *Currency and Banking*, 3-4; Bagehot, *Lombard Street*, Works, V., 112-15.

[2] Mr. Horner himself expressed a modest opinion of the literary merits of the report, but declared that it possessed one great merit, "That it declares in very plain and pointed terms both the true doctrine, and the existence of a great evil growing out of the neglect of that doctrine." Portions of the report were written by Mr. Huskisson and Mr. Thornton, but the inspiring spirit was largely Mr. Horner's. The views set forth were not new and had been so clearly stated by Mr. Ricardo in his pamphlet on "The High Price of Bullion," that some of Mr. Ricardo's friends accused Mr. Horner of borrowing the ideas without proper credit.

[3] *Theory and Practice of Banking*, II., 29.

1. That the mint price of gold bullion, or the legal standard of the coin was, £3 17*s.* 10½*d.* per ounce.

2. That the market price of gold bullion was then £4 10*s.* per ounce.

3. That the foreign exchanges had fallen to an enormous extent: that with Hamburg, nine per cent., that with Paris 14 per cent.

4. That the increase of bank-notes had been very great during the last few years, and was rapidly augmenting.

5. That specie had disappeared from circulation.

The report made by the committee was divided into four parts, the first dealing with the causes of the high price of gold; the second, with the state of the foreign exchanges and the reason why they were adverse to England; the third, with the conduct of the Bank of England in the regulation of its note issues; and the fourth, the increase in circulation of the Bank of England and of the country banks and the increase of their discounts.

The demonstration was easy to intelligent and unprejudiced observers that the high price of gold was the measure of the depreciation of the bank paper. The contention of some of those who declared that bank paper had not depreciated, but that gold had risen in value because of its scarcity, grew out of a muddy confusion of ideas regarding the relations of prices to the two standards of gold and paper. The committee showed that the question of prices had no relation to the difference between the mint price and the market price of gold. The paragraph in which they made this clear is as follows:

> An ounce of standard gold bullion will not fetch more in our market than £3 17*s.* 10½*d.*, unless £3 17*s.* 10½*d.*, in our actual currency is equivalent to less than an ounce of gold. An increase or diminution in the demand for gold, or what comes to the same thing, a diminution or increase in the general supply of gold, will, no doubt, have a material effect upon the money prices of all other articles. An increased demand for gold, and a consequent scarcity of that article, will make it more valuable in proportion to all other articles; the same quantity of gold will purchase a greater quantity of any

other article than it did before ; in other words, the real price of gold, or the quantity of commodities given in exchange for it, will rise, and the money prices of all commodities will fall ; the money price of gold itself will remain unaltered, but the prices of all other commodities will fall. That this is not the present state of things is abundantly manifest ; the prices of all commodities have risen and gold appears to have risen in its price only in common with them.

Another proof that it was not the scarcity of gold, but the depreciation of paper, which increased the market price of gold in paper was the fact "that both at Hamburg and Amsterdam, where the measure of value is not gold as in this country, but silver, an unusual demand for gold would affect its money price, that is, its price in silver ; and that as it does not appear that there has been any considerable rise in the price of gold, as valued in silver, at those places in the last year, the inference is, that there was not any considerable increase in the demand for gold." The committee also called attention to the fact that on previous occasions "the excess of the market price of gold above its mint price was found to be owing to the bad state of the currency ; and in both instances, the reformation of the currency effectually lowered the market price of gold to the level of the mint price." By parity of reasoning, the reformation of the existing paper currency would lower the price of gold to the level of the mint price, without regard to the quantity of commodities which either form of currency might purchase.

The high rate of exchange against England, as expressed in paper currency, was explained by some of the witnesses as being due to a large balance of payment due from England to other countries, either on account of imports of merchandise or expenditures abroad on account of military supplies and subsidies. The committee, however, pointed out that it had "been long settled and understood as a principle, that the difference of exchange resulting from the state of trade and payments between two countries is limited by the expense of conveying and insuring the precious metals from one country to the other ; at least, that it cannot for any considerable length of time exceed that limit.

The real difference of exchange, resulting from the state of trade and payments, never can fall lower than the amount of such expense of carriage, including the insurance." If proof were needed of this simple proposition, it was furnished by the answers given to the searching questions of the committee by Mr. Greffulhe, regarding the actual rate of exchange in coin. "From these answers of Mr. Greffulhe, it appears," said the committee, "that when the computed exchange with Hamburg was 29, that is, from 16 to 17 per cent. below par, the real difference of exchange, resulting from the state of trade and balance of payments, was no more than five and a half per cent. against this country." The committee concluded, therefore, that after making the necessary allowances for the balance of trade and payments, there still remained a fall of 11 per cent. in the exchange with Hamburg "to be explained in some other manner."

Mr. Harman, one of the directors of the bank, declared before the committee, "I must very materially alter my opinions before I can suppose that the exchanges will be influenced by any modification of our paper currency." The committee furnished him in their report the evidence of the depreciation of the Scotch currency, when the optional clause of payment was inserted after the Seven Years' War; the depreciation of Irish currency six years before; and the depreciation of the notes of the Bank of England itself three years after its foundation. The committee then declared:

> Under the former system, when the bank was bound to answer its notes in specie upon demand, the state of the foreign exchanges and the price of gold did most materially influence its conduct in the issue of those notes, though it was not the practice of the directors systematically to watch either the one or the other. So long as gold was demandable for their paper, they were speedily apprised of a depression of the exchange, and a rise in the price of gold, by a run upon them for that article. If at any time they incautiously exceeded the proper limit of their advances and issues, the paper was quickly brought back to them, by those who were tempted to profit by the market price of gold or by the rate of exchange. In this manner the evil soon cured itself.

The committee, in taking up the question of excessive

issues, made the discriminating admission, "that the mere numerical return of the amount of bank-notes out in circulation cannot be considered as at all deciding the question whether such paper is or is not excessive. It is necessary to have recourse to other tests." The economy of money was referred to which had taken place in late years, by "the increased use of bankers' drafts in the common payments of London; the contrivance of bringing all such drafts daily to a common receptacle, where they are balanced against each other; the intermediate agency of bill-brokers; and several other changes in the practice of London bankers." Notwithstanding this, the committee found an approximate increase between 1808 and 1809 of £3,095,340 in country bank-notes, and about £1,500,000 in Bank of England notes. The suspension of cash payments imposed no other expense upon the issuers of this paper than the printing of the notes and some £100,000 in stamp taxes. The committee, therefore, asserted their conclusions, "That there is at present an excess in the paper circulation of this country, of which the most unequivocal symptom is the very high price of bullion, and next to that, the low state of the Continental exchanges; that this excess is to be ascribed to the want of a sufficient check and control in the issues of paper from the Bank of England; and originally to the suspension of cash payments, which removed the natural and true control."

The Bullion Report was presented by Mr. Horner to the House on June 9, 1810, but was not taken up for consideration until May 6, 1811. The debate was opened by Mr. Horner, who spoke for three hours and closed by moving a series of sixteen resolutions. These resolutions declared that when Parliament passed the restriction act, it had no intention that the value of the bank-notes should be altered, but that they had for a considerable time been below their legal value, and that the extraordinary depression of the foreign exchanges was in great part due to the depreciation of the currency of England relative to that of other countries. The final resolutions declared that the only method of preserving the paper currency at its proper value was to make it paya-

ble on demand in the legal coin of the realm, and that cash payments ought to be resumed at the end of two years. The report was ably supported by Mr. Henry Thornton, but was assailed by Mr. Rose, Mr. Vansittart, and others. Mr. Vansittart maintained that "a standard in the sense used by these gentlemen, namely, a fixed and invariable weight of the precious metals as a measure of value, never existed in this country." His idea was that the pound sterling was a sort of intangible thing, and that the paper pound was not to be considered as depreciated so long as it formed the current medium of exchange, and was accepted in the discharge of obligations. The effort was made by the defenders of paper money to deny any difference between gold prices and paper prices, but it was disclosed in the course of the debate that the government themselves were making a distinction by paying guineas to the soldiers in Guernsey at the value of 23 shillings, although their legal value was only 21 shillings.

The country was not ready to return to a specie basis, and Mr. Horner's first resolution was defeated by a vote of 75 in the affirmative to 151 in the negative, and his final resolution by a vote of 45 to 180. Mr. Vansittart followed up his victory by a series of resolutions, to the effect "That the promissory notes of the Bank of England have hitherto been, and are at this time held to be, equivalent to the legal coin of the realm," and that the price of bullion and the state of the foreign exchanges were in no way due to excessive issues of bank paper. Notwithstanding the protests of the better informed members of the House, an amendment by Mr. Canning was rejected, 42 to 82, and Mr. Vansittart's astounding resolutions were carried.

The opponents of the Bullion Report laid stress upon the fact that gold was not sold openly at a premium. The reason was the belief that it was a penal offence to part with a bank-note for less than its face value in bullion, and at the very moment of the debate on Mr. Horner's report three men were lying in prison for selling guineas for more than twenty-one shillings under an old statute of Edward VI.

The issue soon after came before the Court of Common Pleas and they unanimously quashed a conviction under the law and declared that it was no crime to sell guineas at a premium. Lord King in March, 1811, issued a circular to several of his tenants, reminding them that their contract was to pay a certain quantity of the legal coin of the country, and that, as the paper currency was considerably depreciated, he should in future require his rents to be paid in the legal coin of the realm, in Portugese coin of equal weight, or by a sufficient amount of bank-notes to purchase the necessary weight of standard gold. This attempt to establish a gold price distinct from the paper price of commodities caused a tempest of rage among the advocates of a paper currency and led to the charge againt Lord King, so much bandied about in France, of incivism. A bill was promptly introduced into Parliament by Lord Stanhope, making it a misdemeanor to make any difference in payments between guineas and bank-notes. The measure passed the House of Lords by a vote of 43 to 16, and the House of Commons by a vote of 95 to 20.

The disasters to the country banks during 1815 and 1816 greatly reduced the volume of paper afloat and made way for additional issues by the Bank of England. The reduction in country bank paper in circulation is estimated by Professor MacLeod [1] at three times the amount of the issue of the Bank of England, and the effect was immediately felt in the rise in value of Bank of England notes. The market price of gold in paper fell from £5 6*s*., in May, 1815, to £3 18*s*. 6*d*., or within three per cent. of par, in October, 1816. Foreign exchange rose in a corresponding degree, and these rates prevailed until the mid-summer of 1817. The bank had been preparing during the peace in 1815 to resume specie payments and were able after the final overthrow of Napoleon to announce, in November, 1816, that they would pay all notes dated previous to January 1, 1812, and that in the following April they would pay all notes dated before January 1, 1816. Resumption was thus almost accomplished

[1] *Theory and Practice of Banking*, II., 62.

and the people were found to be so accustomed to a paper currency that little demand was made for gold and many persons who had hoarded gold presented it for exchange in bank-notes.

Cash payments were not yet established by law, however, and the restriction had been continued, after Napoleon's return from Elba, until July, 1818. The return of peace brought a great many foreign borrowers to England. Prussia, Austria, and other states were endeavoring to obtain gold to reform their currencies. The result was a heavy drain upon the gold reserve, which had reached £11,914,000 in October, 1817, and the reappearance of a premium upon coin and bullion.[1] Advances to the government were increased from £20,000,000 to £28,000,000 and the bank made no effort to restrict their issues, in the face of the foreign drain and a new increase in the circulation of the country banks. It was perfectly evident that specie payments could not long be maintained with the paper price of gold at £4 3*s*., or about seven per cent. premium, and committees were appointed on February 3, 1819, by both houses of Parliament to inquire into the state of the bank. They reported in favor of a further suspension of specie payments and a bill for the purpose became law on April

[1] The question was much discussed by the orthodox believers of the classical school of political economy, why prices of commodities did not fall with the export of gold and invite foreign purchasers of English merchandise. As Prof. Sumner puts it (*History of American Currency*, 264), "If all nations used specie, or even paper and specie, in only due proportion it would be as impossible for one nation to be drained of specie as for New York harbor to be drained of water by the tide." But all nations do not use specie only, but credit, and modern experience has demonstrated that prices do not move up and down with gold exports and imports, but under the operation of much wider causes in the credit market. The Bank of England did not employ at this time the method of protecting its cash by raising the rate of discount, and the orthodox theory of price movements was of no practical avail against the operation of special causes which drew off gold. See an outline of the discussion in *Money*, by Francis A. Walker, 356–58.

5th. The bill forbade the bank to make payments in gold either for fractional sums or for any of their notes during the session of Parliament. The committees then addressed themselves to a full hearing regarding the bank management and the best means of resuming specie payments upon a secure basis.

The testimony taken by the committees indicated a marked advance in sound opinion among bankers and business men since the adoption of the comic resolutions of Mr. Vansittart. Nearly all the witnesses admitted the influence of the irredeemable circulation upon the foreign exchanges and the necessity of curtailing the circulation when the exchanges became unfavorable and the automatic regulation of redemption in coin on demand was lacking. The majority of the bank directors were not convinced of the wisdom of these views until several years later, but Sir Robert Peel changed his opinion completely and found a powerful supporter in Lord Grenville, who was a member of the Cabinet which originally proposed the restriction act. Lord Grenville went so far as to declare that he considered the restriction one of the greatest calamities under which the country labored and to deplore the part which he had himself taken when it was proposed. While the bank was enabled by the act to lend money with one hand, he declared, it was with the other shaking the foundation of contracts, affecting prices, and involving the country in distress and individuals in ruin ten times greater than any benefits they could derive from liberal issues.

Both houses concurred in the passage of a bill for the gradual resumption of specie payments by the reduction of the mint price of gold. It was provided that after February 1, 1820, the bank should be required to deliver gold of standard fineness in quantities of not less than sixty ounces at £4 1*s.* per ounce; that after October 1, 1820, the rate should be reduced to £3 19*s.* 6*d.*, and after May 1, 1821, to the mint price of £3 17*s.* 10½*d.* per ounce. The provision for payment in bullion was adopted so as to prevent a run upon the bank for coin by small note-holders, while it established

substantial coin redemption when the bullion came to be delivered at the mint price.[1] This liability to pay in bullion was to continue until May 1, 1823, after which full redemption in coin on demand was to be required. The statutes restricting the trade in gold coin and bullion were repealed and Mr. Pitt's practice of free borrowing from the bank was cut off by an act forbidding advances of any description without the express authority of Parliament. It is probable that the bank would have been able to resume cash payments without authority of legislation, within the time which the act required, but its passage by Parliament did much to educate and crystallize public opinion and to protect the bank during the attacks upon the resumption act which were made within the next few years.

The accumulation of gold in the Bank of England was so rapid that it became possible to pass an act in 1821 permitting full resumption on May 1, 1821. The government repaid £10,000,000 of its obligations to the bank and specie payments were resumed in coin at the date fixed by law. The bad harvests and commercial collapse led to several attacks upon the resumption act in Parliament in 1822 and 1823, but they were rejected by large majorities. It was pointed out in the course of the debate that the low price of wheat, which was a great cause of discontent among the agricultural class, could not well be due to the alleged contraction of the currency, for a greater decline had taken place in France, which had been steadily upon a metallic basis, and a like decline in other Continental countries where depreciated paper was still the medium of circulation. The price of wheat at Vienna, in spite of the large volume of the Austrian paper currency, had dropped from 114*s.* in March 1817, to 19*s.* 6*d.*, in September, 1819. It was shown also that the amount of currency in England had increased rather than diminished, for the paper issues had not been materially reduced and a large mass of coin had been infused into the circulation. The only concession obtained by the opponents

[1] Levi, 137.

of resumption was the statute of 1822 (Chapter 70), authorizing country bankers to continue the issue of notes for £1 until the expiration of the charter of the Bank of England in 1833. The permission to issue £1 notes, which had been given to the Bank of England in 1797 and continued during the entire period of restriction, was withdrawn by the resumption acts.

The effect of the monopoly of the Bank of England, which deprived any corporation or large firm of the power to issue notes, but left the power to firms of six persons or less, was the subject of severe criticism every time that the small country banks were swept away in a period of industrial depression. The success of the Scotch banking system was attracting attention and English financiers were desirous of adopting it in England. It was supposed, however, down to 1823, that no joint stock bank could be lawfully established in England because of the exclusive privileges conferred upon the Bank of England by the Act of 1742. It was found, upon careful inspection of the act, and having in view the rule of law that a penal statute must be construed strictly, that the restrictions were limited in their application to banks of issue. The failure to make any distinction up to this time between the power to establish joint stock banks for the purpose of issuing notes and the power to establish them for other purposes was due to the early impression that banking could not be carried on without the issue of notes. The London private bankers had for thirty years suspended the use of circulating promissory notes, but the tradition lingered that joint stock banks could not be established without infringing the legal monopoly of the Bank of England. Mr. Joplin in a pamphlet issued in 1823 announced his discovery that the charter of the bank "does not prevent public banks for the deposit of capital from being established."[1]

There was natural hesitation, even after this discovery, to embark in joint stock banks of deposit without specific authority of law, but the discovery probably had something

[1] MacLeod, *Theory and Practice of Banking*, II., 381.

to do with wringing concessions from the Bank of England and improving the existing system. The government proposed to the bank in 1823 that it consent to the creation of joint stock banks of issue at a distance of sixty-five miles from London, upon condition of the extension of the bank charter for ten years. This proposition was rejected, but the subject was revived after the dreadful panic of 1825. The time for the renewal of the charter was drawing nearer and the bank consented to the Act of 1826, establishing joint stock banks of issue beyond the radius of sixty-five miles from London and requiring the bank to establish branches. These joint stock banks were authorized to issue notes, but they were not to issue them within the prescribed distance nor to draw upon their London agents any bill of exchange payable on demand or for any less sum than £50. A sworn list of the shareholders and places for carrying on business was required of the new banking companies, but few restrictions were imposed as to their management, capital, or cash reserve.

Few joint stock banks were formed for the first few years after the Act of 1826, as the leading country bankers already had private banks and had no wish to set up powerful rivals. The Bank of England managers clung to the monopoly of banking in London, even after they had conceded freedom beyond the sixty-five mile radius, and begged Lord Althorp, when the charter was renewed in 1833, to insert a clause clearly preventing the formation of joint stock banks in the City. Lord Althorp, having obtained the opinion of the law officers of the Crown, in favor of the right to set up deposit banks, refused to impose new restrictions and tartly reminded the directors of the bank that the bargain was that their privileges should remain as they were,—not that they should be extended.[1] A clause was inserted in the Act of 1833, specifically declaring that any body politic or corporate or partnership might carry on the business of banking in London or within sixty-five miles thereof, provided they did

[1] MacLeod, *Theory and Practice of Banking*, II., 384.

not issue notes payable on demand. It was not until after this act that it was seriously attempted to set up a joint stock bank in London. The history of these banks is not a part of the history of banks of issue, but it is an interesting fact that the first was the London and Westminster Bank, which was originally formed as a private partnership and whose manager was Mr. James W. Gilbart, the author of one of the most complete and intelligent works on English banking. Joint stock banks of issue were formed in considerable numbers in the prosperous years preceding the panic of 1836, and more than forty were established in the spring of the latter year. The number issuing notes when the restrictive Act of 1844 took effect was 72, of which only 35 still retain the privilege.

The Bank of England opened its first branches at Gloucester, Manchester, and Swansea. The branches were able to compete on favorable terms with the country banks and to discount bills at four per cent., where the old banks charged five per cent. and sometimes an additional commission. The principal advantage which the country bankers retained was the payment of interest on deposits, but they felt keenly the competition of the branch banks and held a meeting as early as December 7, 1826, to consider it. They adopted resolutions that the establishment of branch banks "have the evident tendency to subvert the general banking system that has long existed throughout the country, and which has grown up with, and been adapted to, the wants and conveniences of the public." A deputation was sent to the Chancellor of the Exchequer, who promised to give serious consideration to their views. Further cause of complaint was found in the stamp duties, which were levied upon the country bank-notes according to value, while a fixed sum was accepted from the Bank of England for their entire issues. The result, according to the country bankers, was to subject them to a tax of £650 on £10,000 where the bank paid only £35. This protest resulted in an act extending the privileges of the Bank of England to the country banks, but the general protests against the branches were

answered by the assurance that "the interest of the country bankers should not be neglected in any negotiation between the government and the Bank of England for the renewal of the bank charter." [1]

The extension of the country banks, without any legal regulation, was popularly regarded as one of the causes of the panic of 1825 as well as of some of the earlier panics. The issue of small notes by the country banks was treated by eminent statesmen as an especially dangerous feature of country banking and as having a tendency to expel coin from the circulation. Many of these notes were retired by the insolvency of the issuers in the panic of 1825 and the ministry seized the opportunity to propose their prohibition for the future. They took steps, without waiting for Parliament to act, to prohibit the issue of the required stamps for £1 and £2 notes and the Chancellor of the Exchequer made an early motion in Parliament that no notes be issued in the future under £5. The proposition became law and after a sharp contest was extended in 1828 to Scotch notes circulating in England.[2]

The approach of the date fixed for the expiration of the bank charter,—at the end of one year's notice after August 1, 1833,—led to the appointment of a committee of the House of Commons May 22, 1832, to consider the privileges to be granted in the extended charter. The witnesses examined discussed the propriety of establishing joint stock banks in London (which most of them opposed), the publications of the accounts of the bank, the regulation of the circulation, and the rate of discount. The subject of making the bank-notes legal tender except at the bank was also considered and the change was urged upon the ground that the notes could then be used by the country banks in the redemption of their own notes in times of panic and the demand for gold diminished. Lord Althorp moved the resolutions for

[1] Gilbart, I., 70–73.

[2] The history of Scotch and Irish banking will show that the effort made at this time, to deprive those countries of the use of small notes, was defeated.

the renewal of the charter on May 31, 1833, and it was decided by a vote of 316 to 83 to proceed with their consideration. The proposition to make the notes legal tender except at the bank prevailed by a vote of 214 to 156.

The new charter continued the exclusive privilege of note issue within sixty-five miles of London, but authorized country banks to have agencies in London for the purpose of paying such of their notes as might be presented. The bank was authorized to reduce its capital by one-fourth of the amount of the debt of the public to the bank and in consideration of its privileges surrendered £120,000 of the amount allowed annually by the government for the management of the debt.[1] The charter of the bank was extended to one years' notice, to be given within six months after the expiration of ten years from August 1, 1834, and until repayment of all debts due by Parliament to the bank. The renewal of the charter in 1844 extended the life of the bank until twelve months' notice after August 1, 1855, and the repayment of the public debt. No such notice was given and the bank continued to operate under this authority until 1870. A revision was made at that time of the statutes relating to the public debt, and it was enacted that the Bank of England shall continue a corporation until all the public funds are duly redeemed by Parliament.[2]

The period following the crisis of 1839 developed a peculiar doctrine of finance in England, which obtained a strong footing among public men with only a rudimentary knowledge of political economy and has spread to some extent on the Continent of Europe and in the United States. This

[1] The government repaid one-fourth of the permanent debt, amounting to £3,671,000, and reducing the principal to £11,015,000; but the bank never availed itself of the permission to deduct the amount from its capital, which remains at £14,553,000, where it was fixed in 1816. The interest on the debt to the bank was reduced in 1892 from three to two and three-fourths per cent., and changes were made in the allowances for managing the debt which made the total saving to the government £45,700.—London *Bankers' Magazine*, July, 1892, LIV., 50.

[2] Clause 72, Act 33 and 34 Victoria, c. 71.

doctrine embodies the ideas that bank-notes are a form of currency entirely distinct from other commercial paper and forms of credit; that an expansion of bank-note issues, even when redeemable in coin on demand, is a potent cause of commercial crises; and that the way to prevent crises is to place fixed limits upon bank-note issues. Few advocates of this theory have undertaken to place definite limits upon the volume of bills of exchange or of other forms of commercial paper issued by solvent borrowers, but they have maintained that bank-notes were money for all practical purposes of daily use; that an undue expansion in the volume of money has stimulated speculation and expelled gold under the operation of Gresham's law; and that the curtailment of note issues would maintain sobriety in the mercantile world and restore the equilibrium of the foreign exchanges.

The advocates of this view, of whom the most conspicuous were Sir Robert Peel, Lord Overstone, and Colonel Torrens, named their new discovery "The currency principle," and immediately set out to rescue the commercial world of Great Britain from future disturbance by enforcing their policy in a modified form upon the Bank of England. Sir Robert Peel declared, in advocating the resumption act of 1819, that it was impossible to prescribe any specific limitation of issue for the bank and that the quantity of circulation which was demanded in a time of confidence varied materially from the amount required in a period of despondency. He became a complete convert to the currency principle in 1844 and introduced the bill which became the basis of the present charter of the Bank of England. The theory of the currency principle was so generally accepted as a means of putting an end to panics that amendment was refused by the House of Commons by a vote of 185 to 30, and the bill passed the House of Lords without a division, and received the royal assent on July 19, 1844. The bill absolutely cut off the creation of banks of issue, except by the union of existing banks, and made the future elasticity of English currency dependent upon deposits of coin or bullion with the Bank of England.

The new charter provided for the separation of the issue department from the banking department of the Bank of England and placed the issue department under the charge of a committee of the directors appointed by the entire body. The Governor was directed to transfer to the issue department on August 31, 1844, securities to the value of £14,000,000, of which the debt due by the government to the bank was to be a part. The bank was also to deliver to the issue department such of the gold coin and bullion as was not required for the banking department and was to receive back a quantity of notes which should make the circulation of the bank exactly equal to the coin and bullion on deposit, plus the sum of £14,000,000 represented by securities.[1] Thenceforth the issue department was to pay coin and bullion for notes and issue notes for coin and bullion, and no department of the bank was authorized or permitted to issue notes in excess of the limits thus established. The price of gold at the bank was fixed for the future at £3 17*s.* 9*d.* per ounce. Weekly accounts of the circulation were to be transmitted to the government and published in the *London Gazette*. The bank was required to pay £180,000 annually for its privileges instead of the rate of £120,000 fixed in 1833. This payment was modified in 1861 and now amounts to about £200,000.

The purpose of fixing the amount of notes covered by securities at £14,000,000 was to economize that amount of gold without impairing the convertibility of the note. The amount was arrived at, not with any special regard to the capital of the bank or the government debt already held, but with regard to the smallest amount of Bank of England

[1] Whether the notes constitute a prior lien on the securities and bullion in the issue department is a point which is not clearly set forth and has never been judicially decided. The act directs that "there shall be transferred, appropriated, and set apart by the said governor and company to the issue department securities to the value of £14,000,000"; but "it shall be lawful for them to diminish the amount of such securities," which seems to preclude the idea that they are not part of the general assets of the bank.—Price, 65.

notes which could be counted upon to remain always in circulation. It was found that the net circulation in December, 1839, was £14,732,000, and it was argued that at least £2,000,000 more must be kept in the banking reserve of the bank. It was considered safe, therefore, to fix the uncovered circulation at £14,000,000 and it was left to the play of the foreign exchanges to control the fluctuations above that amount.[1] Gold imported under the attraction of low prices and high interest rates would be brought to the bank and exchanged for notes, under the theory of the framers of the act, and gold withdrawn from the country by the attraction of low prices and high interest rates elsewhere would be taken from the bank by the presentation of notes, which would thus be withdrawn from circulation.

The principle of issuing notes covered by other securities than coin, within the safe maximum limit of the amount which can be kept permanently in circulation, is a simple and intelligible banking principle, and indeed the principle upon which modern banking is founded. The declared purpose of the act—"to cause our mixed circulation of coin and bank-notes to expand and contract, as it would have expanded and contracted under similar circumstances had it consisted exclusively of coin,"—also seemed simple and intelligible to those who ignored the existence of credit and the domestic causes which made a larger circulation desirable at some periods than at others. The Act of 1844 proposed substantially to destroy the bank-note as an instrument of credit and make it a mere certificate of coin, leaving to other forms of commercial paper the functions which the bank-note had in part performed. It is obvious, however, that the framers of the act, in fixing a maximum limit of authorized circulation, meant to deal only with the conditions then existing and that, if their theory had proved operative, they could not have objected to a much higher limit to meet the expanded volume of modern trade.

Existing private and joint stock banks of issue were permitted, with the usual respect of English law for vested

[1] Mr. Torrens, quoted by Hankey, 5-8.

rights, to continue their outstanding circulation. It was the purpose and expectation that these banks would gradually be led to retire their circulation and remit the power to the central bank of issue. Provision for this contingency was made by the authority given the bank to increase the amount of securities in the issue department to an amount not exceeding two-thirds of the country bank-notes withdrawn and to issue circulation against the new securities.[1] The new issues did not fall to the bank automatically, but required an order from the Crown in Council. The amount of circulation allowed the country banks was determined by the average circulation during the twelve weeks preceding April 27, 1844, and the amount was found to be £5,153,417 for the 207 private banks and £3,478,230 for the 72 joint stock banks. It was not until December 13, 1855, that any increase was made in the secured circulation of the Bank of England. Forty-seven banks with aggregate issues of £712,623 had ceased to issue their notes since the Act of 1844 and an order was made authorizing the increase of the Bank of England issue by £475,000. The next increase was £175,000 in 1861, and the next £350,000 in 1866, increasing the issues upon securities to £15,000,000. An increase of £750,000 was made April 1, 1881; £450,000 September 15, 1887; £250,000 February 8, 1889; and £350,000 January 29, 1894. The secured circulation since the latter date, therefore, has been £16,800,000 ($84,000,000). The lapsed issues since 1844 have been £2,902,997 on the part of 143 private banks, and £1,504,028 on the part of 37 joint stock banks, making a total of £4,407,025.

No provision was made for strengthening the security of the issues of private banks, except the absolute limit put

[1] The limitation to two-thirds of the cancelled issues was based upon the theory that these issues had been protected by one-third their amount in bullion, which would be released for circulation, thus keeping the amount of circulation intact. The utter disregard of banking principles embodied in the law is indicated by this assumption, which completely ignores the necessity for a reserve against general liabilities.—Gilbart, II., 121.

upon the amount, for it was not intended to foster their development. A banker who ceased to issue his own notes was not permitted to resume the issue, and if two or more banks became united and the number of partners of the united bank exceeded six their power of note issue was to cease. The country bankers were required to permit their books to be inspected by a government officer, but this was apparently to prevent an excess of issue rather than to afford any other sort of security to the public. The country banks have been slow to leave the field, as the figures of their circulation demonstrate. Fifty-six private banks were still issuing £2,220,048 and 35 joint stock banks were still issuing £1,974,202 in notes at the beginning of 1896, more than half a century after the beginning of the operation of the Act of 1844. The notes of the country banks were not made legal tender and the banks were not required to publish their accounts.

The operation of the Bank Act of 1844 was put to an early test by the crisis of 1847 and the result was a complete failure upon two essential points. The operation of the act neither prevented the speculation which is the cause of panics, nor reduced the issue of notes to correspond with the export of gold. Inquiries were made by both the House of Commons and the House of Lords, at the meeting of Parliament after the panic and the friends of the Act of 1844 made an earnest effort to rescue it from the discredit which the panic had cast upon it. The committee of the House of Commons reported in favor of continuing the act in effect, but the House of Lords' committee spoke in severe terms of its operation. The failure of the act in the important respect of preventing commercial convulsions was frankly admitted in the debate in the Commons by Sir Robert Peel. It had neither "put a check on improvident speculation," in the language of the Lords' committee, nor afforded "security against violent fluctuations in the value of money." The law was framed to arrest commercial expansion by limiting the means for carrying on commercial transactions. It failed absolutely in this object, because such operations can

be carried on, and usually are carried on, by other means than bank-notes. It succeeded in checking the expansion only when other forms of credit had been swept away by distrust and expansion of note issues to fill their place was absolutely needed to prevent overwhelming commercial disaster. It did not prevent expansion, in simple terms, when expansion might do harm ; it prevented it absolutely when it might have done good.

It was the theory of the supporters of the act, that the currency would fluctuate in exact accordance with the fluctuations of a metallic currency by the self-acting provision for the issue of notes only in exchange for gold and the issue of gold in exchange for notes. Both sides in the discussion of the bill, when it was pending in Parliament, seem to have made the incredible blunder of overlooking the fact that gold could be obtained by the presentation of checks. This was exactly what happened in 1847 and the effect upon the outstanding note issues and the bullion in the bank at different dates during the April pressure is indicated in the following table :

	NOTES HELD BY THE PUBLIC.	NOTES IN THE BANKING RESERVE.	BULLION IN THE BANK.
Aug. 29, 1846	£20,426,000	£9,450,000	£16,366,000
Dec. 19, 1846	19,549,000	8,864,000	15,163,000
Jan. 9, 1847	20,837,000	6,715,000	14,308,000
Feb. 20, 1847	19,482,000	5,917,000	12,215,000
Mar. 20, 1847	19,069,000	5,419,000	11,232,000
Apr. 10, 1847	20,243,000	2,558,000	9,867,000

The bank, therefore, saw its bullion decreasing on the one hand and its banking reserve decreasing on the other hand, while gold and notes poured out of the banking department in the discharge of its obligations. The banking reserve was chiefly in notes which had been obtained by the surrender to the issue department of such gold as was received on deposit, but the payment of these notes to customers either swelled the note circulation or reduced the gold in the bank, by just the amount of the payment. The effect, as Mr. John Stuart Mill pointed out in his testimony before

the Committee of the House of Commons, was a double action, which required each department of the bank to take measures for self-protection and made the bank's action on the money market "as violent on a drain of three millions, as would have been required on the old system for one of six."[1] The banking department might be completely wrecked by the exhaustion of its note reserve, without the power it formerly possessed to draw upon the whole resources of the bank for help.

It was fortunate in many respects that the Act of 1844 failed to operate to contract the domestic circulation as was expected. Such an event would only have added to the intensity of the panic and made the suspension of the act and the issue of additional notes more imperative. Such contraction and such absence of expansion as actually occurred invited a run upon the bank for gold and notes which would not have occurred under former conditions. Bank of England notes were a legal tender except at the bank and were largely employed in the reserves of the country banks. The absolute limit on the supply had the double effect of frightening the public into withdrawing their deposits from the banks for hoarding before the supply was exhausted and of driving the banks to withdraw their deposits from the Bank of England for hoarding against this demand by the public. If they could not get notes under such circumstances, they would take gold, and the reduction of the note circulation in the meantime would only have increased the pressure. The demand for notes, so long as their convertibility was unquestioned, was, of course, immensely increased by the destruction of credit. Hoarding operated to reduce the visible quantity of notes at the very moment that the disappearance of commercial paper as a medium of circulation increased the necessity for them. The terrible pressure thus applied by the Act of 1844 to the commercial community compelled the sale of goods and securities in foreign markets at any sacrifice which would bring the ready currency withheld by

[1] *Political Economy*, B. III., Ch. xxiv., Sec. 4.

the operation of the Bank Act. The operation of the law, therefore, meant an absolute loss, not merely in the nominal sense of money denominations, but in the real sense of surrendering more English commodities for a given quantity of foreign commodities than would otherwise have been required. [1]

The chief contention which was left to the friends of the Act of 1844, after the rude disillusionment of the panic of 1847, was that the act had maintained beyond doubt "the convertibility of the note." They argued that under former conditions and in previous panics, the bank had been drained of gold as well as of its banking reserve, the two not being then separated, and that the ultimate redemption of the notes in gold had been threatened. From a practical point of view, there was perhaps some force in this claim in behalf of the act. [2] The claim is subject to the two conditions, however, that a better knowledge of the rules of banking had come into operation since the earlier panics and that theoretically the "convertibility of the note" was not perfectly assured. It is doubtful, indeed, if convertibility could have been maintained if there had never been, either in 1847, 1857, or 1866, any suspension of the Bank Act. Loss of convertibility would not have come primarily from distrust of the notes or of the credit of the bank, but from the pressure for money by depositors upon the private banks and joint stock banks which kept their reserve with the Bank of England. They would have come upon the bank with a rush for the payment of their deposits and the point might very soon have been reached where the bank had only public securities as

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[1] Gilbart, I., 345–46.

[2] Mr. Mill insists that the convertibility of the note "would have continued to be maintained, at whatever cost, under the old system," and remarks that the suspension of the banking department, "involving, as it would, the probable stoppage of every private banking establishment in London, and perhaps also the non-payment of the dividends to the national creditor, would be a far greater immediate calamity than a brief interruption of the convertibility of the note." —*Political Economy*, B. III., Ch. xxiv., Sec. 3, note.

the guarantee of its circulation. The effort, in other words, to keep the bank standing a solitary monument of unimpaired credit when every other part of the credit system of the country had fallen a mass of ruins around it could not have succeeded. This was the logical meaning of the propositions of those who insisted that the Act of 1844 maintained "the convertibility of the note," so far as they had any definite meaning, and it was a proposition which was utterly chimerical.

If the limitations of the Act of 1844 have been of any value to the English people, it has probably been in driving them to the adoption of substitutes for circulating notes and to the extension of deposit banking. England was sufficiently far advanced in 1844 in the use of instruments of credit to make the restrictions of the Bank Act of much less importance than such restrictions would have proved in a new and undeveloped country. One of the devices adopted in London for promoting the movement of capital was the Cheque Bank. Money was received by this bank on deposit, and books of checks were issued for even denominations, which might be filled in for less than the denomination but not for more. The face value of the checks issued did not exceed the depositor's credit, so that the receiver of such a check had the assurance of the bank that the depositor's account was not overdrawn. Such checks were made payable by the Cheque Bank only through some other banker and not at the counter of the bank, thereby escaping the prohibition of the law against promissory notes payable to bearer on demand. The checks passed between individuals for cash and the Cheque Bank established relations with some 1500 domestic and foreign banks which agreed to receive and cash its checks. Several railways and other companies received these checks as cash and they proved convenient for transmission through the mails.[1] The Cheque Bank, therefore, put in operation a sort of emergency currency, outside the law, if not in violation of law, which has been resorted

[1] MacLeod, *Theory and Practice of Banking*, II, 374–75.

to in other countries only under the pressure of commercial distress.[1]

A much more important and scientific step than cast-iron rules of circulation was adopted by the Bank of England for the protection of its gold reserve after the crisis of 1857. This step consisted in raising the rate of interest rapidly by degrees of one per cent. at a time, instead of fractions of one per cent., in order to arrest the export of gold. The increasing ease and cheapness of communication had destroyed the value of differences of a fraction of one per cent., when this fraction was divided into fractions of a year, in attracting gold from foreign countries or arresting its departure. The theory of statesmen and students of political economy had generally recognized up to this time only two causes of the export of gold—payments for merchandise and the pressure of a depreciated currency. The bullion brokers, without spending time over theories, had long since learned by observation that it became profitable to export gold when interest rates abroad were higher than at home. They fabricated bills of exchange, had them discounted by bankers, took the proceeds in gold and shipped the gold to the point where it would earn the highest interest. The bills fabricated for this purpose had the character of accommodation bills, in that they represented no merchandise transaction and were drawn for the single purpose of transferring money from the place where it was cheap to the place where it was dear, in order to earn the higher rate of interest.

The fact and possibility of such shipments of gold do not seem to have been known, or at least fully understood, up to this time, by the staid old merchants who formed a majority of the board of directors of the Bank of England. The necessity of meeting the drain by rapid advances in the rate of discount was first set forth in the literature of political economy by Prof. H. D. MacLeod,[2] was quickly adopted as the true theory by Mr. Goschen, and put in force by the bank

[1] For a similar device in Austria, see the closing portion of Chapter ix.

[2] *Theory of Credit*, II., 813–18.

which, on this occasion, according to Mr. Bagehot, "and as far as I know, on this occasion alone," made "an excellent alteration of their policy which was not exacted by contemporary opinion, and which was in advance of it."[1] The results were even more striking than were anticipated by the advocates of the new theory, and are thus summed up for the next few years by Mr. Bagehot:

> The beneficial results of the improved policy of the bank were palpable and speedy: we were enabled by it to sustain the great drain of silver from Europe to India to pay for Indian cotton in the years between 1862 and 1865. In the autumn of 1864 there was especial danger; but by a rapid and able use of their new policy, the Bank of England maintained an adequate reserve, and preserved the country from calamities which, if we had looked only to precedent, would have seemed inevitable. All the causes which produced the panic of 1857 were in action in 1864; the drain of silver in 1864 and the preceding year was beyond comparison greater than in 1857 and the years before it; and yet in 1864 there was no panic. The Bank of England was almost immediately rewarded for its adoption of right principles by finding that those principles, at a severe crisis, preserved public credit.[2]

The great expansion of English banking after the middle of the century led to serious doubts as to the capacity of the Bank of England to maintain commercial credit in every conceivable emergency. Mr. Bagehot pointed out in his celebrated work, *Lombard Street*, more than twenty years ago, that the entire fabric of English credit rested upon the gold reserve of the Bank of England. The reserve had then increased somewhat above its level in earlier times, but was still considered by many as affording an insufficient protection for the great volume of the banking business of the country. The private and joint stock banks made no effort to maintain a coin reserve of their own, for such a policy would have locked up their capital and driven them to the wall in the fierce competition for fractional profits. They carried only such cash as was needed from day to day for ordinary transactions, and relied upon their deposits with

[1] *Lombard Street*, Works, V., 118.

[2] For a temporary failure of the new rule to act, and the reason for it, see account of the crisis of 1866, in Ch. xxi.

the Bank of England for cash to meet emergencies. The system thus created was graphically called "the one reserve system," and under it the credit of the entire business community depends upon the solvency of the Bank of England.[1]

Private deposits with the bank were £9,000,000 in 1844; they were £18,000,000 in 1872; they were £50,295,171 for the week ending October 6, 1895. The growth in the deposits of the joint stock banks and private bankers has been equally rapid. They were £120,000,000 in 1872; they are probably £200,000,000 in 1896. These deposits include such of the funds of the country banks as are deposited with the private and joint stock banks, but they do not include the additional obligations of the country banks to their depositors.

The experience of three crises since the Bank Act of 1844 has given serious warning of the shock which would come to every British interest if the Bank of England should prove inadequate to support the fabric of British credit and to supply all foreign demands for gold. Mr. Bagehot fixed "the apprehension minimum," below which the bank reserve could not go without exciting alarm, at £10,000,000, and he maintained that measures to protect the reserve should begin to be taken when it dropped below £15,000,000. The reserve was gradually strengthened by the accumulation of gold and by the financial blunders of other countries until it stood in 1891 at £22,295,403; but this expansion no more than kept pace with the expansion of credit and did not diminish apprehension for the future. Mr. Goschen, the distinguished financier who has several times acted as Chancellor of the Exchequer, proposed a plan in 1891 for issuing £1 notes upon a reserve consisting of four-fifths gold and one-fifth securities. The purpose of the plan was to substitute the notes for gold in the hands of the public, and to draw

[1] The Irish and Scotch banks of issue hold gold funds, which amounted on October 5, 1895, to £8,810,739, but this gold is more or less tied up by the laws governing their circulation, and calls are almost invariably made for gold upon the Bank of England in times of stringency.

the gold into the bullion reserve of the bank. Mr. Goschen proposed, if the bullion in the bank was raised by this means to £30,000,000, to "give certain additional powers of issue in times of emergency," by authorizing the bank to strengthen the reserve in the banking department by the issue of additional notes against securities, on paying to the government a high rate of interest, to be fixed by law.[1] Mr. Goschen's proposals were much discussed, but did not result in definite action.

Recent events have changed the entire face of the problem by strengthening the reserve beyond all past precedent and removing any fear that it will not be adequate for all demands. The chief of these events has been the enormous production of gold in South Africa, which has been flowing into the Bank of England for the past two years at a rate never equalled in its history. The bullion in the bank rose at the end of December, 1894, to £32,547,000, and had increased on January 1, 1896, to £44,960,056. The bullion now exceeds the note issues by fifty per cent., is equal to nearly 75 per cent. of the deposits and post-bills in the banking department, and is equal to about fifty per cent. of the combined liability for note issues and deposits. The influx of gold has been so rapid that the question is already being discussed, whether the effect will not be to stimulate speculation and to burden the country with a mass of dead stock which is not really needed for monetary purposes. The necessity of suspending the free coinage of gold, in order to limit the circulation, has already been suggested by Mr. W. R. Lawson, who discusses the effect of the recent additions to the bullion fund in the following terms:[2]

> A forty-three million gold reserve has become the dominant factor in a financial situation altogether abnormal, the peculiar characteristics of which decline to be judged by the rules or traditions of the past. Revolving round this huge gold reserve, and reflecting all its fluctuations, we have a growing plethora of loanable capital, unwieldy masses

[1] Letter to the governor of the bank, Dec. 3, 1891. London *Bankers' Magazine*, LIII., 2–3.

[2] London *Bankers' Magazine*, October, 1895, LX., 492–93.

of deposits in banks and other financial institutions, where they have next to no productive value; an insatiable demand for high-class investments, which has driven prices up to a dangerous level; a great wave of speculation spreading from one market to another till the entire business of the country seems likely to be infected soon with the morals of the Kaffir circus; a prolonged depression in all the legitimate industries of the country, agricultural and manufacturing; our foreign markets nearly all upset by currency agitations and experiments, which reduce international exchange to a daily and hourly gamble; our domestic industries transferred from private hands to joint stock companies, which have revolutionised all the old methods and ideas of business. Facility of financing has been the principal factor in these transformations, and anything which helps or encourages facility of financing, must accelerate the economic crisis we are passing through. Nothing could act so powerfully in that direction as loading up the Bank of England with gold, which it is obliged to turn at once into loanable capital, thereby diminishing the loanable value of all pre-existing capital of the same class.

The measure of the changes in the bullion in the bank in recent years, as well as the state of the other leading items of the bank's accounts, for the average of the last quarter in each year, is given in the following table:

YEA	NOTES IN CIRCULATION.	DEPOSITS.	SECURITIES.	BULLION.
1880	£26,829,000	£31,350,000	£34,839,000	£26,406,000
1881	26,237,000	28,633,000	37,096,000	20,876,000
1882	26,351,000	27,410,000	36,147,000	20,751,000
1883	25,683,000	29,205,000	35,669,000	22,355,000
1884	25,222,999	29,346,720	36,336,691	20,360,721
1885	24,621,423	29,344,372	34,643,349	20,826,856
1886	24,691,913	27,038,698	33,895,673	19,929,836
1887	24,209,867	26,930,149	32,508,224	20,238,539
1888	24,405,030	29,281,524	35,977,745	19,455,412
1889	24,460,836	29,837,081	36,301,144	19,712,368
1890	24,732,153	35,414,155	39,168,647	21,820,279
1891	25,510,059	34,830,397	38,607,719	23,159,668
1892	26,039,500	34,367,453	36,809,048	24,991,060
1893	25,778,436	34,204,021	35,543,067	25,865,721
1894	25,528,878	41,614,576	32,937,638	35,262,470
1895[1]	26,458,425	56,526,619	48,922,039	44,960,056

The Bank of England is governed by a court of twenty-four directors, and a governor and deputy governor who serve for a term of one year. The senior director who has

[1] Average for week ending January 1, 1896.

not already served is usually made governor and the next in seniority deputy governor. A part of the directors retire every year, but these are usually the younger ones, so that the older always remain. It is customary to choose young men for vacancies in the board, so that they will be still in the possession of physical vigor when their turn comes to be governor.[1] Bankers in the strictly English sense, lenders of money for short terms on commercial paper, are not allowed to serve on the board of directors, but this rule does not exclude the leaders of finance who are engaged in other branches of the banking business. It is usually about twenty years from the time of a man's entry upon the board of directors until he is reached in his turn as governor, and it is rarely that a director is made governor out of his turn or serves more than one year. The board meets with the governor and deputy every Thursday in what has become historic as "the bank parlor," to pass upon the report for the week. The branches of the bank are limited to a few leading cities, and a large share of the business of the bank is derived from the deposits of the private banks and joint stock banks.

The Bank of England has been comparatively free from government interference since the time of Pitt. It receives the public deposits and performs many financial operations for the government, but it differs from many Continental banks in the sense that "it is purely the banker of the state, and not its cashier, and as such maintains with it the same relations as with the individuals and companies which constitute its clientage."[2] There is no division of profits with the state and only moderate taxes are paid. The private and joint stock banks which issue notes are so similar in character to those without circulation that the statistics are rarely separated. The number of banking offices open in Great Britain at the close of 1894 was 5612, of which 477 were in London and the suburbs, 3538 in other parts of England and Wales, 15 in the Isle of Man, 1011 in Scotland, and 571 in Ireland.

[1] Bagehot, *Works*, V., 136.

[2] Noel, I., 232.

The total resources of all the banks of the United Kingdom of Great Britain and Ireland, including banks of deposit merely as well as banks of issue, are over £1,000,000,000. The banks of deposit have of late years become more and more in the habit of making public their accounts, until all but an insignificant proportion now do so. These returns have been compiled for the close of 1894 and early part of 1895 by Mr. R. H. Inglis Palgrave,[1] and show an aggregate capital of £85,629,366; reserve fund, £37,896,899; deposit and note liability, £721,371,206; cash in hand and on short notice, £185,146,719; and discounts and advances, £446,269,821. The aggregates include the Isle of Man, with banking resources of £1,992,856. The figures for the greater divisions of the United Kingdom are given below, those for Scotland representing entirely banks of issue:

LIABILITIES.

	ENGLAND AND WALES.	SCOTLAND.	IRELAND.
Capital paid	£69,121,115	£9,302,000	£7,101,251
Reserve fund	29,037,525	5,694,879	3,064,695
Acceptances, endorsements, etc.	16,919,018	3,105,473	166,492
Deposits, current accounts, and note circulation	570,138,259	100,538,870	48,921,672
Miscellaneous	3,961,744	957,889	471,598
Total	689,177,661	119,599,111	59,728,708

ASSETS.

Cash in hand and on short notice	£158,833,302	£17,343,954	£8,756,180
Brit. Gov. investments	83,497,584	14,281,452	6,899,170
Other investments	66,787,340	20,683,795	9,710,780
Discounts and advances	351,044,075	60,826,034	33,326,566
Acceptances, etc.	16,919,018	3,105,473	166,492
Buildings, etc.	12,096,342	3,358,403	869,520
Total	689,177,661	119,599,111	59,728,708

[1] London *Bankers' Magazine*, April, 1895, LIX., 529.

One of the criticisms which has been made upon the operation of the Act of 1844 is the great number of changes in the discount rate which have taken place at the Bank of England since that time. The criticism is not directed against the propriety of the changes when they have been made, but against the underlying causes which have made them necessary. The fact that England is the centre of the exchanges of the world and feels the pressure of the demand for gold and silver from every quarter has undoubtedly had much to do with these changes, but it has been pointed out that they have not diminished in frequency since Paris has regained some of the exchange business she lost during specie suspension and Berlin has become an important money market.[1] Changes in the rate of discount are preferable to a dangerous reduction of coin reserves and are the modern method of checking such reductions, but a uniform rate has the advantage of offering steady conditions to legitimate industry. The "one reserve system," as well as the peculiar pressure put upon the Bank of England by the Act of 1844, have been charged with a part of the responsibility for the frequent changes in the discount rate, and this view is supported by the few changes since the increase of the bullion in the bank. The present official rate is two per cent. and loans are made below the official rate to customers of the bank, according to long established practice. This rate was adopted on February 22, 1894, so that for nearly two years it has remained unchanged,—an interval without precedent in the history of the bank since the effect of changes in the rate came to be fully understood. The great number of changes between 1845, after the Bank Act took effect, and the close of 1891, in comparison with those in other countries, is shown in the following table[2]:

[1] R. H. Inglis Palgrave, before Institute of Bankers, March 2, 1892. London *Bankers' Magazine*, April, 1892, LIII., 551.

[2] *London Bankers' Magazine*, May, 1892, LIII., 723.

	TOTAL NUMBER OF CHANGES.	RISES.	PER CENT. OF TOTAL.	FALLS.	PER CENT. OF TOTAL.
Bank of England	354	166	47	188	53
Bank of France	101	43	43	58	57
Bank of Germany	130	62	48	68	52
Bank of Holland	153	76	50	77	50
Bank of Belgium	161	71	44	90	56

CHAPTER VI.

THE SCOTCH BANKING SYSTEM.

Its General Scope and Results—The Bank of Scotland and the Royal Bank—The Failures of the Ayr Bank, the Western Bank and the City of Glasgow Bank—Advantages of Scotch Banking and its Effect upon the Habits of the People and the Prosperity of the Country—Branch Banks in London and Limited Liability.

THE Scotch system of banks of issue comes nearer to the ideal of successful free banking than that of any other country. Absolute freedom in note issues reigned for over one hundred years in Scotland, and during eighty years of that period general distrust of the banking system never occurred, small notes became the favorite medium of exchange among the people, and the deposits in the banks absorbed almost the entire savings of rich and poor and brought within the circle of active producing capital the entire accumulations of the country. Such defects as were disclosed in the early years of Scotch banking were corrected with experience, and the few departures which have taken place from sound principles have been such as to suggest no change in the established practice of the majority of Scotch banks, but, at the most, some official regulation which should hold all to the rules voluntarily adopted by the oldest banks and the soundest bankers. The mania for restricting note issues which swept over the British Parliament in 1844 shut the circulation of the Scotch banks within fixed legal limits, and limited the banks of issue to those already in existence, but left untouched their power to issue small notes and their means of accommodating the people of Scotland by receiving deposits.

Banking in Scotland was inaugurated by the system of monopoly, but differed from all earlier banking systems enjoying monopoly of note issues in the fact that the first joint stock bank was formed by private persons for the express purpose of promoting trade and not for supporting the credit of the government. The charter of the Bank of Scotland, which was organized under authority of an act of the Scotch Parliament of July 17, 1695, was framed to some extent on the model of the charter of the Bank of England and made it illegal for any other company to set up the business of banking for twenty-one years. The joint stock was to be 1,200,000 Scotch pounds, the equivalent of 100,000 English pounds sterling, and was to be subscribed in amounts of not less than £1000 Scotch nor more than £20,000 Scotch (equivalent to £83 6*s.* 8*d.* and £1666 13*s.* 4*d.* English).[1] The bank was allowed to lend on real or personal security at not more than six per cent., but was prohibited from employing its stock or profits in any other trade or commerce, except that of lending and borrowing money upon interest and the negotiation of bills of exchange. The company was prohibited from purchasing land or from advancing money to the government, upon the anticipation of any sums to be granted by Parliament, except those upon which a loan should be authorized by a specific act.

The Bank of Scotland soon encountered the opposition of the African Company, otherwise known as the Darien Company, which was organized by William Paterson, the founder of the Bank of England. The Bank of Scotland had so little confidence in its ability to protect its monopoly, that it made no serious effort to contest the legal rights of its rival, but endeavored to strengthen its position by calling in two-tenths of its capital, of which one-tenth had been originally paid in. The African company issued notes with great imprudence, lent to its own shareholders, and was obliged to

[1] The coinage of Scotland was assimilated with that of England by the act of Union in 1707, and the Bank of Scotland assisted in the operation by receiving the old money and giving new money or their own notes in return.

abandon the field in May, 1698. The Bank of Scotland repaid to their shareholders the two-tenths of the capital called in and continued for several years without a rival. No deposits were received at first from the public, but notes were issued against the capital of the denominations of £5, £10, £20, £50, and £100. Notes for £1 were first issued between 1699 and 1704. A run was begun in December of the latter year, which compelled the bank to suspend specie payments. A meeting of the proprietors was held and a device adopted which is still of interest because it is similar to the existing laws of Canada and Germany in the case of failed banks. This device consisted in making the notes bear interest until they were paid and resulted in keeping the notes at par. Payment was made with interest in less than five months, by means of a new call upon the proprietors for one-tenth of the nominal capital. Another run upon the bank was made in September, 1715, when the rebellion on behalf of the Stuarts broke out, and the withdrawal of coin by the presentation of the notes was encouraged by the bank directors in order to prevent the seizure of the coin reserve by the insurgents. The bank suspended payment after most of the cash had been withdrawn and gave notice again that the notes would bear interest until paid. The monopoly of banking for twenty-one years expired in 1716 and no steps were taken to renew it.

The second successful bank in Scotland was formed, as in the case of the Bank of Venice and Bank of England, by the proprietors of the public debt, which they assumed on the union with England. An act which was passed in 1719 empowered the King to incorporate the proprietors of the debt into a body corporate, which was organized in 1724. The new corporation endeavored to secure admission to the Bank of Scotland, upon the terms of increasing the capital of the united bank by the sum of £250,000,—the principal of the debt,—and the division of the annual interest of £10,000 in the proportion of two-sevenths to the shareholders of the bank and five-sevenths to the holders of the debt. The bank was making dividends which were declared by rivals to

run as high as fifty per cent., and they replied that they had no legal authority to increase their capital, that their stock was large enough for the banking business of the country, and that they would not in any case unite with the holders of the debt at par while their stock was worth at least ten per cent. and the debt only paid four per cent. The holders of the debt, or the Equivalent Fund, as it was called, then petitioned the King for banking powers, which were granted on May 31, 1727. These powers were not granted without powerful opposition from the old bank, whose defenders declared that their capital, which they had called in to the amount of three-tenths, making an aggregate of £30,000, was sufficient to circulate all the credit that could be required in Scotland. The last call made for the payment of capital was partly paid in the notes of the bank. This raised a great outcry from unthinking persons, who maintained that the payments should be made in specie, but they were answered by the scientific statement that "bank-notes are justly reckoned the same as specie when paid in on a call of stock, because, when paid in, it lessens the demand on the bank."[1]

The new bank was known as the Royal Bank of Scotland and began business on December 8, 1727, with a capital stock of £151,000. They received support from the government by the deposit of £20,000 of public monies and their business rapidly extended. The Royal Bank is entitled to the credit of the invention of cash credits, the unique feature of Scotch banking which has done so much to promote the prosperity of Scotland and to place business success and wealth within the reach of the humblest of her people. There was a deal of friction between the two banks during these early years and the Bank of Scotland introduced a clause into their notes making them payable at the discretion of the directors at the end of six months, with the interest from the time of presentation until the time of payment, instead of payable in coin on demand. This practical suspension of redemption on demand resulted in excessive

[1] MacLeod, *Theory and Practice of Banking*, II., 203.

issues of notes, not only by the two leading banks, but by private banking and manufacturing companies, and the fall of the notes below par. The attempt to maintain coin redemption was carried out by a process, which is described in detail by Adam Smith,[1] of collecting coin through London agents and sending it down in wagons to Scotland. Bills of exchange were constantly drawn upon London to cover coin obligations and their payment was often provided for only by drawing fresh bills. The fact that the bank paper was below par led to the constant presentation of notes for redemption and justified Smith's declaration that "bringing gold into the country was like pouring water into a sieve, or like the toil of Danaides." The two principal banks soon saw the folly of this method of doing business and agreed to combine their influence to obtain an act of Parliament, which was passed in 1765, prohibiting the issue of notes with the optional clause, making all such notes payable to bearer on demand, and prohibiting notes under twenty shillings ($5).

The Bank of Scotland and the Royal Bank were the only chartered banks until the incorporation of the British Linen Company at Edinburgh in 1746. This company was organized for the purpose of promoting the linen industry by lending money to the manufacturers and as the Company was thus led into the banking business it soon found it expedient to continue as a banking company only, under the original name.[2] The next important institution founded was the Ayr Bank, which distinguished itself by a radical departure from the methods of the older Scotch banks. The wonderful expansion of Scotch agriculture and industry after the failure of the Jacobite rebellion, under the stimulus of conservative free banking and the system of cash credits, was not rapid enough for certain restless spirits who wished to borrow far beyond their capital or credit. The Ayr Bank was formed with the avowed purpose of adopting a more liberal policy, and the course of the older banks in gradually

[1] *Wealth of Nations*, Book II., Ch. ii., 1, 302.
[2] Cunningham, II., 350.

curtailing the discounts of a group of speculators who were dealing in accommodation paper drove all this class of business to the new bank. The result was the over-issue of notes, which came back so rapidly upon the bank for redemption in coin that it was necessary to draw constantly upon London and to incur heavy expenses for commissions and interest. As Adam Smith describes the operations of the bank:

> When it was obliged to stop, it had in the circulation about £200,000 in bank-notes. In order to support the circulation of those notes, which were continually returning upon it as fast as they were issued it had been constantly in the practice of drawing bills of exchange upon London, of which the number and value were continually increasing, and, when it stopped, amounted to upwards of £600,000. This bank, therefore, had in little more than the course of two years advanced to different people upwards of £800,000 at five per cent. Upon the £200,000, which it circulated in bank-notes, this five per cent. might perhaps be considered as clear gain, without any other deduction besides the expense of management. But upon upwards of £600,000 for which it was continually drawing bills of exchange upon London, it was paying, in the way of interest and commission, upwards of eight per cent., and was, consequently, losing more than three per cent. upon more than three-fourths of all its dealings.

The Ayr Bank was founded by a company which comprised the Duke of Hamilton and many other wealthy landed proprietors and it was supposed that their estates, which were pledged by the unlimited liability of the stockholders, would suffice to maintain the notes of the bank at par and supply it with coin. The failure of the experiment proved two of the essential principles of a banking currency—that no greater volume of notes can be maintained in circulation than the convenience of business requires, and that landed security is not the equivalent of coin in maintaining the redemption of notes on demand or the credit of a bank. The period of the operation of the Ayr Bank was one of extensive speculation and large Scotch exports, but the apparent prosperity was brought to a sudden halt by the crisis of 1772, which began in London on June 10th, and caused a run upon

the Edinburgh branch of the Ayr Bank just one week later. The bank continued its payments until June 25th, when it was compelled to suspend and its great mass of obligations was discredited.

The Bank of Scotland was authorized in 1774 to double its capital stock, and began in this year the policy of establising branches which has become so striking a feature of Scotch banking. Efforts had been made in 1696 and again in 1731 to establish branches in Glasgow, Aberdeen, Dundee, and one or two other places, but in both instances proved unprofitable and were abandoned after a year or two. The capital of the Bank of Scotland was increased in 1784 to £300,000, in 1792 to £600,000, in 1794 to £1,000,000, and in 1804 to £1,500,000, of which £1,000,000, was paid in. The present paid up capital is £1,250,000 and the nominal capital £1,875,000. The capital of the Royal Bank has been raised to £2,000,000, all of which has been paid in. The capital of the British Linen Company is £1,000,000, all paid in. The Commercial Bank was founded in 1810 as the banking institution of the Liberal party, with a paid-up capital of £1,000,000, which was strengthened later by a reserve fund of £400,000. The nominal capital is now £5,000,000. These four banks—the Bank of Scotland, the Royal Bank, the British Linen Company, and the Commercial Bank—are the oldest institutions now in existence. The other banks of issue which were in operation when the Act of 1845 forbade the extension of the system were for the most part founded as late as 1825, the date of the foundation of the existing National Bank of Scotland and the Abderdeen Town and County Bank. There were a few older institutions which have since ceased to exist, among them being the Perth Banking Company, founded in 1766 and united with the Union Bank in 1857, and the Dundee Banking Company, founded in 1763 and united with the Royal Bank of Scotland in 1864.

The strength of the Scotch banking system was illustrated by the events which followed the suspension of specie payments in England. The news reached Edinburgh on March

1, 1797, and a meeting of the bank officers decided that it would be necessary for the Scotch banks to follow the example of the Bank of England. There were symptoms of a run for a few days, and the disappearance of specie led to the cutting of £1 notes into quarters to afford a currency for small transactions.[1] The Lord Provost called a meeting of the principal inhabitants, who resolved to support the credit of the banks and to receive their notes as specie. Banks which had been in the habit of issuing notes were allowed to issue notes for five shillings for a limited period and confidence quickly returned. No action was ever brought against the banks for their failure to pay specie, the notes were received as confidently as ever, and in a short time business activity was resumed and continued throughout the long Napoleonic wars. The banks, in the language of the report to the Lords in 1826, "supported themselves from 1797 to 1812 without any protection from the restriction by which the Bank of England, and that of Ireland, were relieved from cash payments."

The policy of the English Bank Act of 1844, to suppress the evils of speculation by restricting bank-note circulation, was extended to Scotland in 1845,[2] but several of the provisions regarding the Scotch banks differ from those affecting the English banks. The banks of issue existing in Scotland at the time of the passing of the act were allowed to retain an authorized circulation equal to the average during the year ending on the 1st of May, 1845. They were also authorized to issue additional notes when fully covered by deposits of coin at the head office or principal place of issue. Not more than one-fifth of this coin deposit was to be in silver. The Scotch banks, therefore, stood upon an equality in issuing notes upon deposits of coin beyond the authorized limit, while the English banks except the Bank of England were absolutely limited. No new bank of issue could be founded, however, in Scotland. The authorized circulation of the Scotch banks, as ascertained under the new law,

[1] MacLeod, *Theory of Credit*, II., 601.

[2] 8 and 9 Victoria, c. 38.

was £3,087,209. The limit of authorized circulation was reduced by the suspension of the Western Bank in 1857, which had an authorized limit of £337,938, and the similar suspension of the City of Glasgow Bank in 1878, which had an authorized limit of £72,921. These reductions fixed the authorized circulation at £2,676,350, where it now stands. The union of two Scotch banks is permitted by the Act of 1845, and the retention of the aggregate circulation of both. Several unions of this kind have taken place without changing the limit of the authorized circulation for the Kingdom. The average circulation of the Scotch banks for the four weeks ending November 30, 1895, including that covered by coin, is shown in the following table:

BANK.	AUTHORIZED CIRCULATION.	AVERAGE CIRCULATION FOR FOUR WEEKS.	AVERAGE GOLD AND SILVER HELD FOR FOUR WEEKS.
Bank of Scotland.....	£343,418	£1,157,369	£1,038,432
Royal Bank of Scotland.....	216,451	1,000,968	950,441
British Linen Company.....	438,024	922,221	630,989
Com'l Bank of Scotland.....	374,850	998,986	768,312
Nat. Bank of Scotland.....	297,024	899,120	756,871
Union Bank of Scotland.....	454,346	1,039,304	777,853
Aberdeen Town and Co. Bk.	70,133	336,625	307,902
N. of Scotland Banking Co..	154,319	484,739	372,944
Clydesdale Banking Co.....	274,321	783,969	625,474
Caledonian Banking Co.....	53,434	141,260	99,806
Total.....	2,676,350	7,764,561	6,329,024

The average circulation shown consisted of £5,170,831 in notes of denominations under £5 and £2,593,730 in notes for £5 and more.

The history of Scotch banking was comparatively uneventful after the restrictive legislation of 1845, except for the two great failures of the Western Bank in 1857 and the City of Glasgow Bank in 1878. As these failures have sometimes been treated by the opponents of Scotch banking as an impeachment of its safety and success, they are worthy of some attention in detail. Both occurred in years when

other banking institutions and business houses in England and other parts of the world were collapsing, but both were the result of methods of banking so reckless and unsound that they had repeatedly received, before the failures, the condemnation of other Scotch bankers. The Western Bank was founded in 1832 and in the twenty-four years of its operation lost its entire capital of £1,500,000, and nearly as much more from its other assets. The Western Bank from the outset kept in London a reserve which was much inferior to that of other Scotch banks and was so small that its drafts were dishonored in 1834 by its London agents. The other Scotch banks thereupon refused its notes and remonstrated with it for its mismanagement. The directors notified the other banks on October 30, 1834, that they had resolved to invest in marketable securities a sum sufficient to secure themselves in the future, to lessen their discounts, and to keep sufficient funds to meet their obligations. The chartered banks, upon this pledge, advanced £100,000 to the Western Bank to enable them to purchase the proposed securities. But the management of the Western Bank soon forgot their promises and returned to their former method of business. These methods were so objectionable that when they applied to the Board of Trade in 1838 for a grant of letters patent, the other banks presented a joint memorial against the grant. This memorial declared that Scotland, during the periodical convulsions among the banks of England, which had led to the failure of several hundreds, had for the most part maintained a state of general tranquillity. The memorial continued :

> The cause of this is notoriously owing, first, to the large capital employed in the Scotch banks, and, second, to the system of administration adopted. Capital alone, as has been recently experienced in England, by extending the scale of operations, may only increase the mischief. In the like manner a numerous proprietary, constituting a protection to the public against eventual loss, may, by adding to the credit, add to the power of such an institution for evil. The safeguard of the Scotch system has been the uniform practice adopted of retaining a large portion of the capital and deposits invested in government securities, capable of being converted into money, at all

times and under all circumstances. This requires a sacrifice, because the rate of interest is small, and, in times of difficulty, the sale involves a loss, but it has given the Scotch banks absolute security, and enabled them to pass unhurt through periods of great discredit. . . .

The Western Bank was established in the year 1832, and the principle on which it has avowedly acted has been to employ as much as possible of its capital and assets in discounts and loans, retaining only the cash necessary to meet its current engagements. . . .

It will be quite apparent that a bank that can employ its whole funds in this manner is enabled either to divide a larger share of profits than its competitors, or to do business on more favorable terms; and we repeat, that if the only consequence of this was to increase or diminish the dividends of the rival establishments, it would be of comparatively small importance, but in its results it endangers the existence of every bank in the country and the fortunes of a large portion of the community. We feel that, if letters patent shall be granted to this bank, after what has passed, it will be a public sanction and countenance of a new and mischievous principle, opposed to the banking system of Scotland.

The charter was not granted and as the result of keeping such small reserves in London the Western Bank was again in trouble in 1847. The bank was then compelled to borrow £300,000 of the Bank of England in November and December, which it repaid in March, 1848. A somewhat more cautious policy was pursued until 1852, when the discounts of the bank were £13,525,332 and the re-discounts were £407,143. The bank even at this time had £356,000 in overdue bills and held a number of life insurance policies as security for dead loans, on which it was paying the premiums. A reckless policy of re-discounting was begun in 1852 which expanded the re-discounts in 1856 to £5,407,363 with ordinary discounts of £20,410,884. The most alarming feature of the bank's affairs, however, was loans to four firms which reached an aggregate of £1,603,725. The character of the bills discounted for these firms is shown by the fact that of £402,716 in bills of Macdonald £398,349 were dishonored at maturity, and the results for the other three firms were only a little better. The books of the bank were examined, soon after the general meeting in June, 1857, by request of the directors and it was found that bad

debts to the amount of £573,000 were carried as good assets and that the advances to shareholders amounted to £988,487. It was found that the four firms to which such immense advances had been made had been dealing in accommodation paper and that the Macdonalds drew upon 124 acceptors, of whom only 37 had been inquired about and 21 were reported as extremely bad. The banks stopped the accounts of these firms, which immediately failed, and a panic resulted on the Stock Exchange on October 10th. Depositors began to withdraw their accounts, the bank was unable to settle its balances through the clearing house and on Monday, November 9th, closed its doors.

The collapse of the City of Glasgow Bank in 1878 was similar in its character to that of the Western Bank twenty-one years earlier and was due to similar causes. The City of Glasgow Bank was compelled to stop temporarily in 1857 and continued to be suspected of reckless management from that time until its failure. The institution had fallen into such discredit early in 1878 that the bill brokers generally asked and received an extra quarter or half of one per cent. over the market rate charged other banks in discounting its acceptances.[1] Distrust finally came to a head in September, 1878, when the London banks found increasing difficulty in getting rid of acceptances sent them by their correspondents in India and ordered their agents in the East to buy no more such paper. The directors of the City of Glasgow Bank appealed to the other Scotch banks for help towards the close of the month and an expert accountant was set to work upon their books. A slight examination showed that nearly £6,000,000 had been lent to four firms and that the books had been deliberately falsified for not less than three years. The other banks declined to give any assistance and the City of Glasgow Bank stopped payments on Wednesday, October 2d. The news was received very quietly in Scotland and the other Scotch banks announced that the notes of the failed bank would continue to be accepted as usual. They also made an arrangement by which relief was given

[1] Gilbart, II., 400.

to depositors who were hampered by the locking up of their money pending the settlement of the bank's affairs.

The heaviest burden of loss fell upon the shareholders, whose liability was unlimited under the law then in force. The liquidators were compelled to institute a number of suits to fasten the liability fully upon the shareholders and to defeat attempts to transfer stock. Having adjusted the list, they made a call for £500 for every £100 of stock held, and subsequently made another call for £2250 per share of £100. The result of the first call, of which the nominal amount was £4,200,000, resulted in receipts of £2,409,066 at the end of the second year of the liquidation, October 22, 1880. The nominal amount of the second call was £7,814,000, upon shareholders who were still solvent, and the amount realized was £3,405,452. The result of these two calls, with a sum of £5,851,657 realized from the assets, enabled the payment of seventeen shillings in the pound within less than two years and payment in full was made within little more than a year, with the help of an advance from the other Scotch banks, to creditors willing to forego interest on their claims. While the creditors thus lost almost nothing, the great majority of the shareholders were absolutely ruined. The majority expressed their purpose at the first meeting on October 22, 1878, to keep faith with their creditors, and they kept the pledge so well that when the two calls had been made the holders of only £88,722 out of the capital of £1,000,000 remained solvent. Criminal proceedings for the falsification of the books were begun against the directors and they were given short terms of imprisonment.

The narrative of the transformation of the unlimited banks of Great Britain into limited companies relates to English banking so far as it affects some of the great English joint stock banks, but it belongs more properly to the history of Scotch banking in its origin and in its relations with important banks of issue. The agitation of the subject was the direct result of the terrible losses suffered by the stockholders of the City of Glasgow Bank because of their unlimited liability for the obligations of the bank. The law of

England, which prevailed in Scotland after the union, presumed and enforced unlimited liability upon corporations except in the cases where special charters had been granted. There was much opposition to extending the principle of limited liability to private partnerships, but a statute of 1855 (Chapter 133) finally authorized the formation of joint stock companies under such conditions. Joint stock banks were excluded from the operation of this law and the exclusion was continued in the joint stock banking act of 1857. The failures of that year led to an enactment of 1858,[1] which admitted banks to the privileges of limited liability so far as concerned their general obligations. Banks issuing promissory notes, however, were liable for the amount of the notes, without limitation, in addition to the sum for which they might be liable to general creditors. This act was merely permissive and required banking companies which took advantage of it to give thirty days' notice to each customer and after registering under the act to post conspicuously at their offices, on February 1st and August 1st of each year, a statement of their liabilities and assets.

The Act of 1858 would have averted the hardships of the stockholders in the City of Glasgow Bank if they had taken advantage of its provisions before the failure. The three older Scotch banks, however, held special charters which limited their liability and the others, aside from the natural indisposition to revise their constitutions, feared that the effect would be injurious to their credit. Thus matters remained until the collapse of the City of Glasgow Bank. Investments in bank shares were recognized by the law courts in Scotland as a legitimate investment of trust funds, but the trustees were personally liable for the calls made by the banks as well as to their clients, and many were ruined by the failure. A steady selling of shares began all over England and Scotland, by the prudent as well as those who were carried away by the flurry of the moment.[2] The shares of the three senior Scotch banks declined about £55 on an

[1] Statute 1858, c. 91.

[2] Gilbart, II., 433.

average, while the shares of the unlimited banks fell about £90.

The subject of permitting banking with limited liability under different conditions from those imposed by the Act of 1858 was brought up in Parliament and the government on April 21, 1879, introduced a bill for the purpose. The act became law [1] after a good deal of controversy and authorized the increase of capital stock by an amount equal to existing shares or some multiple of their value, and liable to be called up only in case the company was wound up. This constituted a reserve liability, which placed a definite fund within the reach of a failed bank without requiring assessments upon the shareholders to the full amount of the liabilities. The principal of unlimited liability was retained in regard to note issues by corporations whose original charters were unlimited. Most of the leading English banks and the unlimited Scotch banks soon registered under the new law. It was feared that the adoption of limited liability would result in a reduction of deposits, but this fear was discovered to be unfounded and deposits materially increased in the limited banks within the next few years. The banks generally adopted the policy of increasing their reserve funds by setting aside a part of the profits, but the reserve funds themselves are a source of profit in the revenue derived from the securities in which they are invested. It was found, moreover, by some of the English joint stock banks that a better class of shareholders, of undoubted responsibility, were attracted by the limited principle where men of straw without other visible assets had begun to acquire title to the stock when the liability was unlimited.[2]

The three senior Scotch banks possessed the privilege of limited liability in respect to both note issues and general liabilities. They desired in 1881 to increase their capital and to issue additional stock under the conditions of the limited companies.[3] The bills which they proposed were at first

[1] 42 and 43 Victoria, c., 76.

[2] London *Bankers' Magazine*, June, 1892, LIII., 897.

[3] The chartered banks had occasion to point out, in the course of

favorably received in Parliament, but after passing a second reading in the House of Lords were opposed by the government. Conferences and correspondence ensued which brought out some rather startling statements as to the policy of the government towards the Scotch note issues. Several of the objections made to the proposed bills were completely demolished by the representatives of the banks, and the government several times shifted their position. The government at first objected to legislation by private bill and suggested that the grant of new privileges in recent years to corporations had been accompanied by a review of those already possessed. They declared they were determined to oppose the grant of new powers if the three banks continued to ask for them accompanied by limited liability for notes. The banks promptly offered to cover their note issue by government securities to the amount of the circulation authorized by the Act of 1845 and by coin to the amount of the excess. The government then suddenly forgot their solicitude for the security of the circulation and intimated that they would give the banks a lease of the right of note issue for a fixed term, subject to a moderate royalty.

This was an important indication of public policy, for it grew out of the theory that the right of note issue was peculiarly an attribute of the state. It was based upon a measure dealing with English banks of issue which had been brought before Parliament by Lord Palmerston in 1865, but never became law. The government emphasized their leaning towards state note issues by an alternative proposition which they submitted,—that the banks join them in considering the terms upon which a state issue of notes, conducted through the agency of all the banks, and maintaining the £1 circulation, might be introduced into Scotland in place of the existing circulation. The banks replied

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the discussion which followed, that there were legal difficulties which were almost insuperable against extending unlimited liability for existing note issues to their shareholders, but they expressed their willingness to adopt other safeguards for the ultimate redemption of the notes.—Gilbart, II., 448.

at length, declining these propositions. They did not care to take a lease of rights which they declared were already theirs and had been exercised under express grants from the Crown or from Parliament for from 135 years, in the case of the youngest, to 186 years in the case of the oldest of the three banks. A state issue of notes, they declared, would not be acceptable to the people of Scotland, who would suffer more than the banks from the closing of many of the branches and the diminution of banking facilities which would be the necessary consequence.

The right of the Scotch banks to maintain their branches in England became a subject of active controversy in 1875, when Mr. Goschen introduced a bill in the House of Commons prohibiting such branches. The National Bank of Scotland had established a London branch in 1865 and the Bank of Scotland in 1872, and Mr. Goschen himself had carried through a bill permitting the Royal Bank to do so in 1873. It was the opening by the Clydesdale Bank of branches in Northern England which aroused the hostility of the English banks.[1] Mr. Goschen's bill resulted in a commission, which made no recommendations, and the matter was dropped. A new attempt was made to drag the limitation upon Scotch banking into the limited liability act of 1879. It was embodied in the eighth section of the original government bill and prohibited limited companies from establishing branches outside that part of the Kingdom in which they had their head offices. The Scotch banks were immediately up in arms against this provision and the government were finally persuaded to abandon it. They attempted a flank movement, by cutting down the operations of the bill to the joint stock banks of England, entirely excluding Scotland and Ireland. This was to defeat one of the most important purposes of the bill and the friends of the Scotch banks declared that they would not permit it to pass in such a form. The government were finally compelled to give way and permit its passage in a form applicable to the entire United King-

[1] MacLeod, *Theory and Practice of Banking*, II, 397.

dom and without any limitations upon the power of the Scotch banks to establish their branches in London.

The essential features of the Scotch system of banking have been freedom of note issues, the use of small notes, and cash credits. The great achievements of the system with these elements may be summed up thus:

1. It has provided Scotland with an elastic currency, adapted to the condition of her industries and adequate in volume to their changing needs.

2. It has enabled the people to carry on numerous commercial and agricultural transactions for which they could not have found the necessary quantity of coin and has economized the locking up of capital in the precious metals.

3. It has made the use of notes of small denominations familiar and popular and has taught the people the distinction between bank-notes as the representatives of credit and the precious metals as the measures of value.

4. It has brought into active use the available savings and capital of the country.

5. It has afforded an opportunity for entering upon business to thousands of poor but honest men and enabled them to lay the foundation of a comfortable home and in many cases of a fortune.

6. It has convinced the people so conclusively of the value and safety of the banking currency system that no serious panic has ever lasted beyond a few days or has ever affected any of the banks except those which were justly the subject of distrust.

I. The first proposition, that the Scotch banking system has provided the country with an elastic and adequate currency, is strictly applicable only to the period between 1765, when payment of notes on demand was made obligatory by law, and 1845, when the volume of authorized circulation was arbitrarily limited. The limitation imposed in 1845 could not be seriously objected to at that time, because it left the authorized circulation at the amount then existing. The moderate demands of changing seasons for an increased volume of circulation could easily be met by issues of notes

against coin, since it would be highly improbable and imprudent that any bank should be without a small supply of coin which might be made available for such a purpose. This view of the matter is based, however, upon the theory that the population and trade of Scotland were to remain stationary or to decline, as actually happened to the population of Ireland. An advancing population and volume of trade must gradually feel the fetters cramping the flesh of commerce and this has been to some extent the experience of Scotland. "The only effect of this law," upon the banks, according to M. Courcelle-Seneuil, "has been to limit their productive power, in condemning them to keep in reserve a considerable sum without necessity."[1] Protests against the operation of the Act of 1845 have been frequently made by the Scotch chambers of commerce and experience has seemed to justify the early criticism of Mr. Gilbart, "that restrictions upon banks are taxes upon the public."[2] But Scotland had already passed the point in 1845 where free banking was of supreme importance to her industrial development. Limitations upon her circulation might hamper the operations and reduce the profits of the banks, but they could not unlearn the lessons in saving and in the use of banking facilities which had been taught by a century of free banking.

The Scotch circulation has continued to fluctuate in some degree according to the seasons, the lowest point being reached in March and the highest in November. The advance, however, is not steady from March to November, but rises to a high point in May and then falls slightly until the advance sets in which culminates in the autumn. May and November are the months when the interest on mortgages is usually settled, annuities are paid, the country people take the interest on their deposits, and servants receive their wages. It was the custom during the first half of the present century to settle all such transactions by bank-notes. This made it easier for the banks to keep their accounts than under the system of drawing odd amounts in checks; for a

[1] *Traité des Opérations de Banque*, 298.

[2] *History, Principles, and Practice of Banking*, II., 217.

depositor having payments to make would draw out the entire sum in notes, would receive his payments during the day in the same form, and would deposit the net proceeds again in one sum in notes at the close of the day. The use of checks has now become more general, but does not prevent the rise and fall of the circulation in the autumn and spring as formerly.[1]

The elasticity and security of the Scotch circulation are assured by the daily exchange of notes through the Edinburgh clearing house. The settlements for notes were undertaken at an early date by the Bank of Scotland and the Royal Bank, on each alternate month and are made by exchange drafts on London. A bank which cannot meet the test of these settlements is driven to suspension, as happened to the Western Bank in 1857. The daily exchanges by notes are the great regulator of the paper currency and by their means, according to the admission of one of the most radical opponents of free banking, "the average circulation of Scotch bank-notes is reduced to a term of a few days."[2] Notes which are not demanded by the convenience of trade quickly come back to the banks as deposits on current account and are returned through the exchanges to the issuing bank to be retired and cancelled.

II. The proposition that the banking currency of Scotland has enabled her people to carry on numerous transactions for which they could not well have found the necessary quantity of coin, was abundantly demonstrated by the testimony before the committees of Parliament which made reports upon the subject in 1826. The Act of 1845 was not successful, according to Mr. Gilbart, "in imparting to the people of Scotland a taste for gold." The circulation of notes, with the profit which the banks derived from circulation, was necessary to maintain the existing banking system and afford accommodation to the Scotch people. The banks have never issued the gold except upon demand or for special purposes. When it has become necessary to increase

[1] Gilbart, II., 207, 216.

[2] Wolowski, *La Banque d'Angleterre*, etc., 515.

the circulation beyond the limit imposed by the gold in hand, they have quietly brought the gold from London to Edinburgh and kept it locked up in the vaults of the bank until the necessity for it was at an end. The amount of gold kept in the Scotch banks prior to the legislation of 1845 was but a small percentage of their obligations, but was large enough to maintain their solvency and supply the yellow metal when demanded for export or other special uses. The specie holdings for the four weeks ending January 3, 1846, just after the act took effect, were only £1,180,406, or less than half a pound sterling per capita, against a circulation of £3,336,409. The specie had increased for the four weeks ending March 5, 1864, to £2,337,459 against a circulation of £3,996,743; and for the four weeks ending October 5, 1895, to £5,521,437 against a circulation of £7,054,197.

III. The use of small notes has also been of enormous advantage to the people of Scotland, and has produced none of the dangerous results to the stability of the currency which have sometimes been predicted in other countries when small notes have been proposed. The benefits of issuing notes for £1 were fully set forth in the testimony before the committees of the two houses of Parliament in 1826. Mr. Robert Paul, the Secretary to the Commercial Bank, summed up some of the evils of abolishing small notes by declaring that it would require the reduction of the number of branches, because of the increased expense in the transmission of gold; the withdrawal of cash accounts, because they would no longer accomplish the end for which they were granted,—the maintenance of the small note circulation and the profits derived from it by the banks; and the reduction of the rate of interest paid on deposits, because it would be necessary to keep a very large stock of gold and to keep it wholly unproductive.

A letter written by an agent of the Renfrewshire Bank at Greenock to the manager, Mr. Roger Aytoun, set forth in an even more striking manner the absolute paralysis which would fall upon many transactions by the adoption of a gold

currency and the abolition of notes under £5. Cattle dealers in the country markets, he pointed out, often purchased two or three hundred beasts, reaching an aggregate value of several hundred pounds, but they purchased them by the single animal, at a price ranging from £2 to £4, from the farmers who brought them to market. It would be necessary, if £1 notes were abolished, for them to come to market loaded with gold and silver, and the difficulty of obtaining it from the banks would be increased by the fact that the banks derived no profit from its circulation. Grain was bought up, it was pointed out, in much the same manner and the herring fisheries, which often amounted at Lochfine alone to the value of £40,000 in a single season, were brought in by a thousand boats, whose catch for a night was generally under £5. "If small notes are superseded, and gold substituted," continued the letter, "it is not easy to see how the supply of gold is to be kept up to carry on the business and transactions of this country. Should a quantity of it be received into the circulation, it would not remain long, but find its way into the banks, who will not again give it out in bills as they do their notes, and it will immediately become a scarce article in the country. A person, then, having to pay in small sums, will on every such occasion be obliged to send his large notes to the bank that issued them, perhaps a hundred miles off, to receive gold and silver in their place, to answer his purpose." The evidence was so overwhelming of the value of the small note system that even Sir Robert Peel and the extreme advocates of the currency principle were convinced of the serious injury which its abolition would do in Scotland and both the committees of the Lords and the Commons recommended the postponement of the measure.

IV. The fourth advantage of the Scotch currency system, that it has brought into active use the available savings and capital of the country, is due to the system of allowing interest on deposits. This is hardly practicable except under freedom of note issues, because no other system would afford the banks sufficient profit to pay a rate of interest attractive

to capital. The early regulations permitted deposits for any amount above £10, subject to withdrawal at the will of the depositor and bearing interest from the day of deposit until the day of withdrawal. This system was supplemented by the provident banks, which received deposits of small sums until they amounted to £10. It was the ambition of the Scotch domestic, fisherman, and agricultural laborer to accumulate enough for a bank deposit during a half year or a year and add it to the principal and interest which he had already earned. When this sum accumulated sufficiently to enable the depositor to buy or build a house, or to set up as a master in the trade in which he had been a servant, it would be drawn in bank-notes, which would continue to afford profit to the bank until returned by some other depositor. The system thus stimulated greatly the frugality and savings of the poor, and did much to accumulate in Scotland a capital capable of developing her agriculture and manufactures.[1]

It has not been merely as savings banks, however, that the Scotch banks have contributed to bring into the circle of active industry the entire capital of the country. The wide diffusion of branches under the Scotch banking system places a bank account within the reach of every small trader. The result, in connection with the interest allowed on deposits, has been to create a much greater number of deposit accounts from small tradesmen than in any other country. The facility of banking and the advantage of earning interest have tempted the Scotch tradesman to keep his spare cash in hand at the lowest minimum and to deposit his entire surplus in the bank. The payment of interest thus acts as a direct check upon excessive issues by bringing the notes back to the bank for deposit. The advocates of the Scotch

[1] The proof of the large savings of the Scotch people and their general use of banking facilities may be found in the bank returns for the United Kingdom for 1894 published near the close of Chapter V. These returns show that, in spite of the enormous wealth and banking business concentrated in the City of London, the deposit liabilities of the Scotch banks, divided by the population of Scotland, show a per capita average of about £27, while those of England subjected to a like process show an average of about £22.

banking system blame the English banks for their failure to invite the available capital of the country into their coffers by the payment of interest.[1] If a Scotch banker issues a quantity of notes, he feels assured that nearly all of them will be paid into some bank in the course of the day. There was a competition among issuers, before the Act of 1845, but it was under the restraint of the theoretical rule of free banking, that the notes come back to the bank whenever they are issued in excess. Many of the English banks, however, have discouraged deposits and active accounts by charging a commission when the accounts were operated upon.

Deposit accounts and the payment of interest have thus operated at once to bring within the circle of productive industry every possible fraction of available capital, but they have operated also to apply constantly to the banks the touchstone of a sound and scientific currency,—the redemption and cancellation of their notes. These results could not be accomplished by a great state institution or without the wide diffusion of banks or their branches. The ten Scotch banks of issue have now over 900 offices or branches, or an office for every 4500 people, men, women, and children. The methods by which they have accomplished such results, moreover, are not, in the language of M. Courcelle-Seneuil, "the exercise of a blind routine, the setting in motion of a sort of mechanism; they have been the employment of an enlightened judgment in their loans, the exercise of a high intelligence applied to business." The Scotch system of branches results in an even distribution of capital by withdrawing it from points where it is not needed and concentrating it where it is needed. The branches in the agricultural districts usually accumulate more capital than is needed within their own circuits and transfer it to the manufacturing districts, which are able to employ nearly all the capital they can obtain. This system kept capital within the country and the payment of interest on deposits contributed to deter the Scotch people from the reckless investments which

[1] Gilbart, II., 211.

have absorbed so many millions of English, French, and American money.

It was predicted, when the regulation of note issues was applied to the Scotch banks in 1845, that the result would be the reduction of the interest paid on deposits, and this prediction has been verified by events. A part of this reduction has undoubtedly been due to the accumulation of capital and the fall in its price in the money markets of the world, but a part is due to the increased cost of banking under the Act of 1845. A radical departure was taken from the old methods of Scotch banking, when the banks by a circular of October 1, 1892, gave notice that after that date the allowance of interest on credit or balances of current accounts would be discontinued.[1] No distinction was made in regard to the rate of interest, at the time of the Act of 1845 and for some years after, between deposit accounts and credit balances of current accounts. The rate allowed was the same on the two classes of accounts and seldom fell so low as two per cent. The rate in force on deposits for several years was one and a half per cent. and this was reduced in January, 1895, to one per cent. These low rates have destroyed much of the motive for depositing idle capital in the banks, and have driven the Scotch people to send their money to Australia and seek other and less secure investments than those which they formerly obtained at home by simply depositing their surplus in their current accounts with the banks.

V. The fifth great advantage of the Scotch banking system, that it has afforded an opportunity for entering upon business to thousands of poor but honest young men, is due chiefly to the system of cash credits. The Royal Bank found, soon after its organization, that it had more capital than it could employ in ordinary commercial operations on bills of exchange within the narrow circle of Scotch commerce. The result was the adoption of the system of cash credits for the promotion of agriculture and industry. The system consists in giving an open credit, or drawing account, to a customer who is vouched for by two or more trustworthy

[1] London *Bankers' Magazine*, April, 1893, LV., 577.

persons. A cash credit of £100 authorizes the person in whose favor it is granted to draw upon the bank for that amount, but he is not usually expected to draw the entire sum at once and is charged with interest only on the amount actually drawn and not repaid at any given time. The system differs, therefore, from the discounting of a bill of exchange in the fact that the money can be drawn piece-meal instead of in bulk and interest is charged only upon the portion of the loan actually outstanding. If payments are made from time to time into the bank, they are credited and the interest charged is reduced. The persons who vouch for the holder of the cash credit are called cautioners or sureties.

A cash credit, therefore, is in the nature of permission to overdraw an account up to a fixed limit. Cash credits are rarely given for sums below £100 and generally range from £200 to £500. The banks prefer these small sums, but sometimes grant such credits for £1000 or even larger sums. Payments upon these credits are made in the notes of the bank, which are thus kept in active circulation. Such a credit is not allowed to lapse into a dead loan of the aggregate amount, but it is expected that payments will intermingle with drafts upon it. It is intended as a working capital for men of good character engaged in trade or agriculture. It has the advantage over the ordinary method of loans by discount, not only that it is more economical to the borrower, but that it keeps within the control of the bank all sums not in active business use. The holder of a cash credit is not only benefitted by paying into his account all the cash which he may receive from day to day, but he reduces the bank's outstanding loans by that amount and enables it to increase them in other directions.

The advantage of this system to Scotch industry has been incalculable, measured not only in shillings and pounds to the borrower, but in the stimulus which it has given to the thrift, frugality, honesty, and morality of the people. The two cautioners keep an eye upon the young man for whom they have vouched, have a right to know the state of his accounts, and if they find that his business is badly conducted,

they can withdraw their security and authorize the bank to call in the loan. The losses on cash credits have been trifling throughout the entire history of Scotch banking. Cash credits have been granted to manufacturers and large employers and to the trustees of great public works, as well as to young men setting up in business and to farmers desiring money in anticipation of the sale of their crops. Many distinguished Scotch manufacturers have testified that the system of cash credits was the foundation of their success in life. Mr. Monteith, a member of Parliament who testified before the Committee of the House of Commons in 1826, declared that he was then a manufacturer employing 4000 hands and that, except for the merest trifle of capital which was lent to him, and which he soon paid off, he began the world with nothing but a cash credit. The testimony before the same committee showed that upon one cash credit of £500 there were operations to the amount of £70,000 in a single year, and one witness stated that during twenty-one years in a country bank of moderate size operations took place to the amount of £90,000,000 and that there had been but one loss of £200 on a single account and that the whole loss of the bank during the entire period did not exceed £1200.[1]

VI. The confidence which has been produced among the Scotch people in the system of a banking currency as maintained by their banks was illustrated in a remarkable manner at the time of the failures of the Western Bank in 1857 and the City of Glasgow Bank in 1878. The run upon the Western Bank began on Tuesday, October 13, 1857, and continued for three days, but during that entire period the bank paid away only about £36,000, in coin, and for the entire month from October 10th to November 7th only £44,000. Deposits were drawn out to the amount of £1,280,000, but in nearly every case the depositors were willing to accept the notes of the bank and when it suspended operations the notes in circulation were still £720,000. The heaviest pressure upon the bank came after

[1] MacLeod, *Theory and Pratice of Banking*, I., 347.

the announcement that it would receive support from the other Edinburgh banks on condition of winding up. This pressure came, not from any demand for gold, but from large tradesmen who transferred their accounts to other banks in order to establish banking relations for the future.[1] The bank was unable to settle the heavy exchanges which were thus created against it in the settlement with the associated banks.

It was not until Sunday, November 8th, that the other banks resolved to refuse the notes of the Western Bank in consequence of its inability to settle its exchanges, and the demand for gold became more marked on Monday and Tuesday. The Western Bank closed on Monday and a genuine panic was directed for a day and a half against the City of Glasgow Bank, because it had been guilty of the same negligence as the Western Bank regarding the keeping of its reserve in London. The bank was obliged to close on Wednesday, but the demand for gold was almost entirely confined to depositors and very few note-holders came forward to demand payment of their notes. Large remittances of gold arrived from London on Wednesday and Thursday, the run on the banks ended on Wednesday afternoon, and the people seemed to retain the same confidence as ever in the other banks and received the notes even of the Western Bank when the other banks agreed to again receive them. When the City of Glasgow Bank failed in 1878, it was only necessary for the other banks to announce that they would continue to receive its notes, as usual, to put an end to all uneasiness on the score of the notes. If the banks on these occasions had not been allowed to issue notes, the entire demand for

[1] The same tendency to substitute the note obligations of the bank for a deposit account was shown in British North America after the failure of the Commercial Bank of Manitoba on July 3, 1893. The reason in this case for preferring notes was the fact that they were made by the Canadian banking act of 1890 a perfectly secured first lien upon the assets. The banks receiving these notes were willing to hold them for a time, at the request of the liquidator, because they bore six per cent interest until paid.—Breckenridge, 394–95.

the withdrawal of deposits must have been met in coin and would have put a heavy pressure upon the coin reserves. But the small notes were readily received, the deposit accounts of the solvent banks were not assailed and the Scotch banking system retained as completely as ever the confidence of the people.[1]

[1] M. Horn declares that the three elements which have especially promoted the solidity of the Scotch banks and inspired the public confidence have been their large capital; loyal adherence to commercial banking, without complications with the government; and the system of exchange of notes, which established a sort of mutual supervision.—*La Liberté des Banques*, 424.

CHAPTER VII.

BANKING IN IRELAND.

The Effect of Political and Economic Misfortunes—The Early Bankers and the Foundation of the Bank of Ireland—The Provincial Bank and Other Banks of Issue—The Collapse of the Agricultural and Tipperary Banks—The Act of 1845 and Present Conditions.

IRELAND has had almost as varied an experience in banking as in the political fortunes of her people and her banking history has been affected more or less unfavorably by the agitated condition of the country. The policy of England towards Ireland was distinctly selfish during the seventeenth and eighteenth centuries. Irish agriculture was crushed by the importation of bounty-paid wheat from England and Irish manufactures were stifled by countervailing duties intended to prevent their competition with English goods.[1] The linen trade was almost the only one which was allowed some degree of prosperity, upon the theory that it was better for England to draw her linen supply from a dependency than to pay foreign countries for it. This policy was changed from 1782 to 1800, while Ireland had an independent parliament, for the policy of large bounties and protective duties, and for a brief period Irish industry started forward by leaps and bounds under this artificial stimulus. But the country soon felt the heavy cost of the bounty system and prosperity began to decline before the union with Great Britain. The economic history of Ireland then became a part of that of England, and a reasonable degree of progress was made up to the time of

[1] Cunningham, II., 298, 523.

the potato famine in 1846. That event caused a loss of population by starvation and immigration which has never been recovered. Absentee landlordism also has been a permanent source of loss to the country by the large amount of produce and money annually sent abroad in payment for rents. The fact that bank deposits have increased and that Ireland has retained within her limits a large fund of gold and silver, in spite of these obstacles to her progress, is high evidence of the productive and thrifty character of the Irish people and the sound judgment of their bankers.

The earliest banking in Ireland seems to have been done by brokers or intermediaries, who brought borrowers and lenders together for a consideration. The business of issuing promissory notes against deposits of coin gradually grew up among the goldsmiths and tradesmen, who carried it on in addition to their regular callings. These notes were given a legal status as negotiable instruments by an Act of 1709, which made them assignable and transferable by endorsement. There were no banking laws to prevent fraud and failure, and the losses by the failure of banks or exchangers was estimated as early as 1682 at having been £50,000 within a few years.[1] The Act of 1709 gave the power to protest inland as well as foreign bills and promissory notes for non-acceptance or non-payment. The Irish House of Commons acted as a court of bankruptcy and a special act of Parliament was necessary for the liquidation of the affairs of an insolvent institution. The first act of the kind on record is in 1721, which was passed for the relief of the creditors of Mead and Curtis, a Dublin firm which had suspended on June 14, 1727. A bill for the relief of Burton and Falkiner of Dublin was passed in 1733 but the final legislation regarding the affairs of this firm was not passed until 1757. The firm had acted as bankers for the government and their failure seems to have been due to their large holdings of landed property, which could not be turned into cash when needed.

A series of failures took place in 1755 and 1756, which led

[1] Dillon, 17.

to the appointment of a select committee of the House of Commons to make an inquiry. They reported that credit had suffered by the setting up of persons as bankers without sufficient capital, and recommended that bankers be required to register the real and personal estate which they proposed to hold as security for the payment of their liabilities, that the names of the issuing bankers be stated on bank-notes, that bankers should not be permitted to trade as merchants, and that it should be made a felony without benefit of clergy for cashiers or clerks to embezzle money in excess of £50. The committee also recommended the cancellation of notes at the time of payment. These recommendations, except that regarding the registration of security, were embodied into law in 1755 (29 George II., c. 16). This act did not entirely revive credit and four important banking failures took place in 1758 and in 1760. The first was that of Clements, Malone, and Gore, a firm established on July 3, 1758, which closed its doors on November 1st, of the same year. This firm issued deposit notes payable to bearer on seven days' notice with interest at the rate of ten pence per week for every £100 (two and one-sixth per cent. per annum). The deposits obtained were larger than were expected and were invested largely in land, but the depositors soon began to demand repayment of their notes and as cash could not be obtained the firm was obliged to suspend.[1]

Three of the six large banking firms in Dublin suspended in 1760 and the others refused to discount bills and practically suspended business. Among the firms which remained solvent was that of Messrs. La Touche and Co., which began business in 1725 and survived as a banking house until its fusion with the Munster Bank in 1878. The financial condition of the country and the state of credit were in such a situation that a meeting of the merchants of Dublin was held in April, 1760, which made an appeal to Parliament for relief. A committee of inquiry was named by the House which reported on April 23, 1760, that the quantity of paper in circulation was insufficient to carry on trade and manufac-

[1] Dillon, 23.

tures, and recommended support for the three surviving banks to the amount of £50,000 each. This recommendation was adopted and the notes of these bankers were received as cash in the subscription for a loan which was then being raised. The failure of Sir George Colebrook, Bart., and Company, London bankers who had opened a branch in Dublin, in 1764, was the cause of another panic in 1770 which led the Lord Lieutenant and some of the gentry to issue a notice pledging themselves to receive the notes of the existing Dublin bankers without question.

The effort to found a strong joint stock bank began the year after the foundation of the Bank of England. A number of the principal merchants of Dublin held a meeting in 1695 and presented a memorial to the Irish House of Commons on September 17th, recommending the establishment "of a public bank or a fund of credit, for the encouragement of trade, and supply of the present want of money." The petition was referred to the committee on trade, but was never reported upon. The matter was revived in 1720 by Lord Abercorn, Lord Boyne, and others, who petitioned the King for authority to found a public bank with a capital of £500,000. The Lords Justices reported in favor of the scheme and the King authorized the Lord Lieutenant to grant a commission and charter. The consent of the House of Commons was required for a proper bill and the early stages were favorably passed. Charges of jobbery began to be made against the promoters of the bank, a rival scheme was started with a capital of £1,000,000, whose promoters were charged with paying £50,000 to members of the House as bribes, and the outcome was the passage of a resolution on December 9, 1721, "That the erecting or establishing a public bank in this Kingdom will be of the most dangerous and fatal consequence to his Majesty's service and the trade and liberties of this nation." Religious, political, and financial reasons influenced the action of the House, but a stronger reason was probably found in the infringement of the privilege of originating legislation, which they jealously guarded.

The plan of a public bank remained in abeyance until

1782, when Ireland obtained a new constitution, was freed from humiliating tariff restrictions and believed herself upon the threshold of a new era of prosperity. Mr. Eden, the Secretary to the Lord Lieutenant, presented the heads of a bill for a bank on February 27, 1782. Some opposition developed among the existing bankers and their friends in the House and when Mr. Eden called the bill up on March 5th, the opponents of the bank endeavored to secure an adjournment, but the motion was lost and the report of the committee was agreed to. The capital of the bank was fixed at 600,000 Irish pounds,[1] of which no person was to subscribe more than £10,000, and which was to be lent to the government at four per cent. The charter was to run until January 1, 1794, and until twelve months' notice of withdrawal and the re-payment of all sums due the bank by the government. The bank began business June 23, 1783, and as early as October 31st, of the same year Mr. David La Touche, Jr., was able to inform the House of Commons that great advantages had resulted, particularly to the traders in linen. The first offices of the bank were in some old houses in Mary's Abbey, but after the union of Great Britain and Ireland in 1802, the directors of the bank purchased the Parliament house for £40,000. They remodelled it to meet their requirements and established the bank there in 1808. The meetings of the directors and shareholders are held in the old chamber of the Lords and the general office occupies the old House of Commons.

The new institution was known, in similar language to that establishing the Bank of England, as "The Governor and Company of the Bank of Ireland," and was not allowed

[1] The coinage of Ireland, although bearing the same names, differed from that of Great Britain. The English shilling was passed in Ireland for thirteen pence, although twelve Irish pence were equal to a shilling and twenty shillings to a pound. This made English coins worth about eight per cent. more than Irish coins of the same names and led to much confusion until the currencies were assimilated by the Act of 6 George IV., c. 79, making the currency of Great Britain that of the United Kingdom and providing for the interpretation of contracts in its terms.

to charge more than five per cent. interest on loans and discounts. If the bank incurred debts to a greater amount than its capital, the subscribers were answerable in their private capacity to the creditors in proportion to their subscriptions. The stock was to be transferable and to be deemed personal estate, and as such to go to the executors of the holders rather than their heirs. Fifteen directors were to be chosen annually, not more than two-thirds of the directors of the preceding year were to be re-elected, and the corporation was to have a governor and a deputy governor. The charter of the bank was renewed in 1791 and the capital increased to £1,000,000. Another increase of £500,000 was made in 1791, and still another increase of £1,000,000 was made in 1808 by 48 George III., c. 103. The charter was extended at this time until the expiration of twelve months' notice after January, 1837. The last increase of capital was made in 1820, when the total was fixed at £3,000,000 in Irish currency (equivalent to £2,769,231 in English currency). This last increase was taken from the surplus fund of the bank and lent to the government, making the aggregate loans to this date £2,630,769 in English currency. The total annuity paid the bank by the government was fixed at £115,384, which was reduced in 1845 to £92,076, or at the rate of three and a half per cent. on the English equivalent of the amount of the loan, and was further slightly reduced in 1892.

The suspension of cash payments in England in 1797 was extended to Ireland, without any apparent necessity, "for the sake of uniformity." Exchange was then in favor of Ireland, there was no special demand upon the Bank of Ireland and no drain of gold was feared. The effect of suspension, however, was to enormously stimulate the issue of notes, which increased from £621,917 in 1797 to £2,482,162 in 1800, £3,068,100 in 1809, £4,212,600 in 1813, and finally reached £5,182,600 in 1821 and £6,309,300 in 1825. Exchange turned against Ireland as early as 1804 and led to the special inquiry by the British Parliament which resulted in the formulation of the principles afterwards repeated with

greater elaboration in the Bullion Report. The evidence showed that silver had disappeared from circulation, even for subsidiary purposes, and been replaced by silver notes. Mr. Colville, a director of the Bank of Ireland, testified that there were in Ireland seven bankers issuing notes ; 28 issuers of gold and silver notes, 62 issuers of silver notes ; and 128 issuers of I. O. U's.[1] The Bank of Ireland made large profits upon its forced circulation, and paid dividends never less than six and a half per cent. and rising in 1803 and 1805, including a bonus, to twelve and a half per cent. Exchange on London became favorable after a time, not because the value of Irish currency was raised, but because that of England had fallen to its level.

The substantial monopoly of joint stock banking by means of note issues was conferred upon the Bank of Ireland by the act of incorporation, which declared that it should "not be lawful for any body politic or corporate, erected or to be erected, other than the corporation thereby intended to be created and erected into a national bank, or for any other persons whatsoever united or to be united in covenant or partnership exceeding the number of six persons, to borrow, owe, or take up any sum or sums of money on their bills or notes payable at demand, or at any less time than six months from the borrowing thereof." This provision left it in the power of individuals and firms of small numbers to issue notes, and this privilege was availed of to a great extent after the suspension of cash payments. Nothwithstanding the worthless character of many of these institutions, the demand for currency was so imperative that large quantities of notes were easily floated and great distress occurred, after 1820, when the number of institutions outside the Bank of Ireland had been reduced to six. The Bank of Ireland was permitted by an Act of 1821 (chapter 27) to resume cash payments on June 1st of that year.

The absence of a proper circulating medium, in spite of the monopoly enjoyed by the Bank of Ireland, led to a pro-

[1] MacLeod, *Theory of Credit*, II., 609.

vision in the act which increased the capital of the bank,[1] that the bank should surrender its monopoly outside the circuit of fifty Irish miles from Dublin. Companies of more than six partners were henceforth authorized to do a banking business and to issue circulating notes outside the proposed limit. A party of English capitalists determined to take advantage of this provision and at a meeting in London on June 11, 1824, resolved to found a bank with a capital of £2,000,000 in shares of £100 each, of which one-fourth was to be paid up. Subscriptions were received far beyond the amount needed before the end of the year and the capital of the Provincial Bank of Ireland, which was thus established, has never been increased except in 1836, when £40,000 was transferred to the capital from the "rest" or reserve fund. The monopoly enjoyed by the Bank of Ireland in Dublin made it necessary to keep the head office of the new bank in London, but an agency was established in Dublin and Messrs. La Touche and Company acted as agents until 1838, when the bank opened its own office.

The Provincial Bank rapidly extended its branches throughout Ireland, establishing them at Cork, Limerick, Clonmel, and Londonderry in 1825; at Sligo, Wexford, Belfast, Waterford, and Galway in 1826, and at other towns in successive years. The Bank of Ireland, which had been content with its head office until it found competitors in the field, began a policy of opening branches and established them at Cork, Waterford, Clonmel, Londonderry, Newry, Belfast, and Westport almost as soon as the prospectus of the Provincial Bank had appeared. They began an action of law against the Provincial Bank in December, 1828, because of the payment of the latter's notes in Dublin. The jury found in favor of the Bank of Ireland upon the law and the evidence, but awarded damages at sixpence, with costs of a like amount, as evidence of the feeling in the business community of Dublin against the narrow policy of the bank. The restiveness of the merchants was further indicated in a petition to the Lords of the Treasury for the establishment

[1] 2 George IV., c. 72.

of joint stock banks in Dublin, which led to a compromise. An Act was passed in 1830, making lawful the payment of notes in Dublin by the issuing bank for the purpose of withdrawing them from circulation. The Provincial Bank obtained the privilege in 1827 of receiving the revenues of the excise, stamps, and postal service outside the Dublin district reserved to the Bank of Ireland. Collectors of revenue were authorized in the same year to receive the notes of the bank in the same manner as those of the Bank of Ireland.

The Acts of 1820 and 1825 made it possible to establish joint stock banks in different parts of Ireland and several of these were soon incorporated. The first was the Northern Banking Company, founded by the partners of a private bank of the same name in Belfast. An attempt was made to convert this bank into a joint stock bank in 1820, but it was found necessary to await a change of the law requiring the residence of all the partners in Ireland. The bank began business in its new character in January, 1825, with a capital of £500,000. The capital was increased in 1867 to £1,000,000 and has since been increased to £2,000,000, of which £400,000 has been paid in. The Northern Banking Company purchased the business of Messrs. Ball and Co., of Dublin in 1888 at a cost of £22,500 and opened an office at the capital. The Belfast Banking Company was another institution which was founded upon a private company. It began business as a joint stock bank of issue on August 1, 1827, with a capital of £500,000, of which £125,000 was paid in. The capital was increased in 1866 to £1,000,000 and in 1883 to £2,000,000 with £400,000 paid in.

The National Bank of Ireland was founded in 1835 as the result of the Nationalist feeling in the country. It began business at the Carrick-on-Suir with a subscribed capital of £1,000,000 and consisted at first of separate bodies of shareholders, English and Irish. When a branch was opened, the local share-holders subscribed a portion of the capital and the English proprietors contributed a like amount. The profits were divided evenly between the two interests, but the system proved inconvenient and the stocks were

consolidated in 1837 except in two branches, where the consolidation was delayed until 1856. Daniel O'Connell was the first governor of the bank and his name caused the institution to be dubbed "The Liberator's Bank" and made way for its notes all over Ireland. The only other bank of issue which is still doing business is the Ulster Bank, founded in 1836, at Belfast. The capital was originally £1,000,000, which has since been increased to £2,400,000, with £400,000 paid up. The profits paid in dividends to the shareholders were twenty per cent. annually from 1866 to 1885 and have been only a little less in subsequent years. The Royal Bank of Ireland was established at Dublin in 1836, but was restrained by the monopoly of the Bank of Ireland from issuing notes, and was found in this condition in 1845 by the legislation confirming the power of issue to the banks which then possessed it. The Royal Bank, although a powerful and profitable institution, was, therefore, never enrolled among Irish banks of issue.

The foundation of the National Bank was intended to offset in a measure the collapse of the Agricultural and Commercial Bank of Ireland, which was established in 1834 by the appeals of a Dublin baker, Mr. Thomas Mooney, to the patriotism of the Irish people. Mr. Mooney bore the same name as a Dublin capitalist of wealth and standing and he secured as one of the directors a stationer named James Chambers, which was also the name of a distinguished Dublin financier who was a director of the Bank of Ireland. The impression generally prevailed that these two eminent gentlemen were interested in the new bank and Mr. T. M. Gresham, who was brought into the bank just before its collapse, testified before a committee of the House of Commons that "there is no manner of doubt that we were all deceived in two names in that bank." The capital of the Agricultural Bank was gathered up from all sorts of humble people by appeals to their Irish patriotism and parts of it were obtained by liberal discounts to those who presented commercial bills. A meeting of the shareholders after the collapse of the bank was attended by two steamboat-loads

from Belfast, most of whom had their expenses paid by the directors, and another contingent came from the south of Ireland in canal boats. The branch managers of the bank were selected according to their holdings of stock and acted in reckless disregard of orders from the head office, even to the extent of raising their own salaries and dating the increase back to the time of their appointment.[1] The nominal capital of the Agricultural Bank was £1,000,000, but it was admitted that at the time of beginning business it did not actually exceed £3,000. The first branch was opened at Nenagh, Tipperary County, in November, 1834, and the bank was compelled to close its doors on November 14, 1836. A special act of Parliament was required to wind up the affairs of the bank and an attempt to put it on its feet under a new organization failed in 1841.

The Tipperary joint stock bank, which succeeded Scully's private bank in 1838, did not issue its own notes, but had an arrangement with the Bank of Ireland by which its paper was discounted. The power was reserved to the Tipperary bank by the Act of 1845 to take the same amount of issue as it would have been entitled to in case of the termination of the agreement with the Bank of Ireland, so that it was recognized as connected with the system of banks of issue. The directors of the institution when it became a joint stock bank were John Sadlier, his brother James, and Mr. James Scully. The capital of the bank was £100,000, a portion of which was held in England, and favorable reports were regularly made and large dividends declared for some seventeen years. Prosperity seemed to reign in the affairs of the bank until February, 1856, when the doors were closed, less than a month after the issue of a favorable report and the declaration of a dividend. It was found that John Sadlier had systematically robbed the bank and falsified the accounts. Sadlier was one of the brilliant swindlers who so often take the world by storm and persuade shrewd men of business to embark with them in great enterprises. He had piloted through Parliament several important railway bills, obtained

[1] Dillon, 71–77.

the reputation of immense wealth, been elected member of Parliament for Carlow, and was offered and accepted the position of a Junior Lord of the Treasury. He became chairman of the London and County Bank in 1848, chairman of the Royal Swedish Railway and a director in numerous stock companies. Towards the close of his career he indiscriminately used all the funds of either corporation he could lay his hands on, issued duplicate shares in the railway company and forged documents which he deposited as security for advances from other bankers. His forgeries began to be suspected, the Tipperary Bank collapsed, and on February 17, 1856, Sadlier's body was found by a laborer crossing Hampstead Heath, lying on the ground with a bottle labelled "poison" beside it.[1]

The Banking Act of 1845, following the similar legislation for England and Scotland, repealed the acts of Parliament which prohibited the formation of stock companies for banking with more than six partners. This threw down the bars to all comers, so far as the organization of banks of discount and deposit was concerned, but circulation was put in a straight jacket, as in the case of the English banks. The authorized issue of circulating notes after December 6, 1845, was not to be permitted to exceed, upon an average of four weeks, the average amount of the circulation for the year ending on the first day of May, 1845.[2] If any two banks united, they were allowed to maintain the aggregate authorized circulation of both the old banks, and if any bank surrendered its issue or agreed to issue Bank of Ireland notes, the Bank of Ireland was allowed to increase its issues to the full amount of the notes withdrawn. The law differed in this respect from the English act, which limited the increase in Bank of England issues in such cases to two-thirds of the issues withdrawn.

The Irish law differed in an important respect from the English banking act in regard to the additional circulation which the banks were authorized to issue against deposits

[1] Dillon, 81–86.

[2] 8 and 9 Victoria, c. 37, sec. 19.

of coin and bullion. This privilege was accorded to all the Irish banks of issue,—instead of but one, as in the case of England,—and they were thus put upon an equal footing with no apparent purpose of concentrating issues finally in a single institution. The Irish banks are required, however, to keep the coin held against additional circulation wholly at their head offices, while all their notes are required to be redeemed on demand at the place or places where issued. These requirements compel them to keep a supply of coin at every branch, in order to redeem notes issued from that branch, and it is the practice for a bank to redeem any of its notes at any of its branches where they may be presented. The fact that the privilege of additional issues has been availed of to only a limited extent, while the coin holdings of the banks have been large, would seem to indicate that the fixed limit of authorized issues has not operated greatly to restrain the business development of Ireland. One reason for this is doubtless found in the fact that the population and the volume of business were so greatly decreased in the famine years, while the authorized circulation remained untouched. The limit has proved in practice so generous that Ireland has enjoyed a currency fluctuating with the seasons and with the varying demand for money, in much the same manner as an untrammelled banking currency.

The circulation was nearly £1,000,000 above the limit in 1846, standing at £7,266,000, but declined as low as £4,310-000 in 1849. The average returned in 1854 to £6,296,000 and increased pretty steadily until 1860, when it stood at £6,840,000. A decline then set in, which reached its lowest ebb in 1863 at £5,405,000. Another period of increase carried the average circulation for 1872 as high as £7,674,000, after which it fell to £6,065,000 in 1879, rose to £7,297,000 in 1882 and fell to £5,885,000 in 1887,—the lowest average for twenty years. The authorized circulation of each bank, with the circulation and specie holdings for the four weeks ending November 30, 1895, are shown in the following table:

BANK.	AUTHORIZED CIRCULATION.	AVERAGE CIRCULATION FOR FOUR WEEKS.	AVERAGE GOLD AND SILVER HELD FOR FOUR WEEKS.
Bank of Ireland.....	£3,738,428	£2,670,475	£648,823
Provincial Bank of Ireland..	927,667	801,786	353,299
Belfast Bank.....	281,611	610,087	470,583
Northern Bank.....	243,440	591,926	461,219
Ulster Bank.....	311,079	897,974	708,535
The National Bank.....	852,269	1,356,717	854,549
Total.....	6,354,494	6,928,965	3,497,008

The average circulation shown consisted of £2,896,841 in notes of denominations under £5 and £4,032,124 in notes for £5 and more.

The elastic character of the Irish currency, in spite of the restrictions of law, gives an interest to the fluctuations during the year which result from the varying demand for money. Beginning with January, the amount of the circulation usually declines,—slowly at first, but more rapidly in May, June, and July, until it reaches its lowest point at the end of August. Then begins the process described by Mr. Gilbart, as a consequence of the law that "the monthly circulation must depend upon the quantity of produce brought to market within the month":

> Now, it has been the custom in Ireland to commence bringing the produce to market immediately after the harvest. Hence arises the increase of the notes in September, and their further increase in the following month. But in the beginning of the year the landlords collect their rents, and receive from their tenants the notes for which this produce has been sold; this brings the notes back to the bank, either to be placed to his credit (if he have an account there), or, otherwise, in exchange for a letter of credit on Dublin, or a bill on London. The circuit of a note, then, is this:—It is obtained from the bank by a corn-merchant, who pays it to a farmer for his corn, which he ships to England. The farmer afterwards pays the note for rent to his landlord, who brings it back to the bank.[1]

One of the peculiar features of the Irish circulation, like the Scottish, is the large proportion of small notes. The Select Committee of the House of Commons in 1826 recommended fixing a limit of time in the future beyond which

[1] *The History, Principles, and Practice of Banking*, II., 286.

the circulation of notes below £5 should cease, but the testimony given before the committee was against such a restriction and it was not adopted. The arguments made against the restriction were that it would check the growth of manufactures, make difficult the sale of small lots of agricultural produce, and curtail the accommodation which the banks are able to give their customers and especially their cash credits. The transfer of gold, it was pointed out, would be inconvenient and costly, and once sent out of the country it would rarely come back. The Act of 1845 prohibited notes of fractions of £1 and required the banks in their reports to state separately the notes in circulation under £5. These returns have shown a large proportion of small notes in circulation and a marked increase from September to January over the spring and summer months. This circulation of small notes has contributed, with the widely diffused system of branches,[1] and the existence of several strong joint stock banks without the power of issue, to afford reasonably adequate facilities for the development of banking in Ireland. The proof of the growing use of banking facilities is afforded by the steady expansion of deposits, shown in the following table, in the face of a decreasing population :

YEAR.	POPULATION.	TOTAL DEPOSITS AND CASH BALANCES.	DEPOSITS PER CAPITA.
			£ s. d.
1840	8,155,521	£5,567,851	0 13 8
1847	8,025,274	6,493,124	0 16 2
1850	6,877,549	8,268,838	1 4 1
1855	6,014,665	12,285,822	2 0 10
1860	5,820,960	15,609,237	2 13 7
1865	5,594,589	18,619,000	3 6 7
1870	5,418,512	24,366,000	4 9 11
1875	5,278,629	33,519,000	6 7 0
1880	5,202,648	29,746,000	5 14 4
1885	4,924,342	29,370,000	5 19 4
1890	4,716,996	33,061,000	7 0 2
1893	4,606,527	34,637,000	7 10 4

[1] The number of branches of the issuing banks in 1887 was 353, affording an average of one to 13,000 inhabitants and to 200 square kilometers. Counting the joint stock banks which do not issue notes, the average was one branch to 10,500 inhabitants and to 180 kilometers.—Noel, I. 75. The number of offices of all Irish banks at the beginning of 1895 was 571.

CHAPTER VIII.

THE BANKS OF GERMANY.

The Bank of Prussia and the Share of the State in its Profits—Other Banks of Issue in Prussia and the Smaller States of Germany—The Reform of Currency and Banking under the Empire—The Sales of Silver and the Withdrawal of Paper Money—Absence of Legal Tender Character in the Bank-Notes.

THE existing banking system of the German Empire is a part of the fabric of imperialism which was so industriously built up by Prince Bismarck from the beginning of his premiership in 1862 until his retirement from office. The Imperial Bank of Germany is in a measure an expansion and development of the Bank of Prussia, which was founded in the time of Frederick the Great, but it has already absorbed the circulation belonging to the banks of most of the other German states and is authorized to absorb the entire paper circulation of the Empire as it is surrendered by the local banks, in much the same manner as the Bank of England is authorized by the Act of 1844 to absorb the circulation of the country banks of England and Wales. The circulation of the Imperial German Bank, while modelled in many respects on that of the Bank of England, is capable of a somewhat greater degree of elasticity, by virtue of a legal provision for an emergency circulation above the usual limit, and the notes are not a legal tender.

The Bank of Prussia was created by virtue of an edict of June 17, 1765, under the name of the Royal Bank of Loans and Current Accounts at Berlin (*Konigliche Giro- und Lehnbank zu Berlin*) with a capital of 1,000,000 thalers ($750,000)

and was at first exclusively an institution of state. It continued to be a state institution until 1846, when the new demands for capital for railways and for the extension of commercial relations led to an extension of the scope of the bank and an appeal to private capital to carry it on. Two ordinances of April 14 and July 18, 1846, authorized the increase of the capital by a sum of 10,000,000 thalers ($7,500,000) and admitted the shareholders to a part in the administration by means of a central commission composed of fifteen members, who were authorized to appoint a commitee of three to exercise a regular supervision over the acts of the directors.[1] The capital owned by the State had been increased by the setting aside of profits until it had reached in 1846 1,197,553 thalers ($900,000), and the portion furnished by the public was increased in May, 1856, to 15,000,000 thalers and again by the law of September 24, 1866, to 20,000,000 thalers, ($15,000,000), divided into shares of a par value of one thousand thalers each. The capital credited to the state had been increasing in the meantime until it attained in December, 1867, a total of 1,897,800 thalers ($1,425,000).

The government took care to keep its hands firmly on the direction of the bank, in spite of the new privileges given the shareholders, and limited the right to participate in the general assembly of shareholders to the two hundred holding the largest amount of stock domiciled in Prussia. Supreme control was reserved directly and exclusively to a privy council (*Bank Kuratorium*), composed of the President of the Council of Ministers, the Ministers of Finance, of Justice, and of Commerce, and a fifth member named by the King. The direct management also was confided to a director and a committee of direction appointed upon the King's nomination. This official control was compensated in a measure by exemptions from imposts and from certain taxes which were imposed upon other similar establishments. The bank was compelled, however, to pay interest on the deposit of the public funds and to pay three and a half per

[1] Noel, I., 246.

cent. upon the capital contributed by the State and half the net profits remaining after the payment of a dividend of a like amount to the shareholders. The receipts of the government from these sources, including interest on its own stock, attained a very considerable figure during the eight years prior to its transformation into the new Imperial Bank, amounting to 3,166,436 thalers in 1873; 1,711,920 thalers in 1874; and 2,284,875 thalers in 1875.

The accounts of the Bank of Prussia afford a good illustration of the principle that banks of issue usually precede mere banks of discount and deposit as a means of familiarizing the public with banking methods. There were scarcely any deposits in the early history of the bank, except those made by the government and upon which interest was paid by the bank. These government deposits came from the trust funds of the courts, including those of guardianship, and the administration of churches, schools, hospitals, and other charitable foundations and public institutions. Their magnitude constantly grew and their use by the bank gave it loanable funds which it could not otherwise have obtained except by an issue of notes upon commercial paper disproportionate to its original capital. This money entrusted to the bank enabled it to do a discount business which steadily grew with the expansion of commerce in Prussia and among her neighbors. The aggregate of the discount business of the year rose from 1,581,956,399 marks ($395,000,000) in 1867 to 2,630,469,468 marks in 1871, 3,958,299,756 marks in 1872, and 5,350,216,312 marks in 1873. The business depression which began in the latter year forced the discounts down to 4,136,089,162 marks in 1874 and to 4,099,613,175 marks ($1,025,000,000) in 1875.

One of the peculiarities of the Bank of Prussia, which extended to many other German banks, was the practice of making loans upon merchandise as well as upon bullion and the pledge of securities. Business of this kind was always kept within conservative limits and the statutes of the Bank of Prussia admitted the precious metals at a valuation of only 95 per cent. of their real value and merchandise at

from 50 to 60 per cent. The valuation of negotiable securities was determined by the officers of the bank. All these operations were limited in amount and were required to run for terms no longer than bills of exchange, for which the maximum was three months. The number of loans of this sort steadily declined during the latter years of the history of the bank, while the amount increased, reaching a maximum in 1872 of 824,840,690 marks ($206,000,000), including securities.

The issue of circulating notes was the chief means by which the Bank of Prussia was able to utilize its assets and there was no limit of law after 1856 upon the volume of the issues. The law of 1846 forbade the issue of bills for a greater sum than 21,000,000 thalers ($15,750,000), but the repeal of this provision in 1856 left the bank untrammelled, except as the opinion of the banking community imposed a relation of one to three between the metallic reserve and the circulation. The bills were not a legal tender and were redeemable in coin on demand, but they were accepted in public depositories by virtue of a royal ordinance of June 9, 1847. The denominations were limited to ten, twenty-five, fifty, one hundred, and five hundred thalers, equivalent to a minimum of $7.50 and a maximum of $375. A further limitation was imposed that bills of the smallest denomination should not exceed a total of 10,000,000 thalers ($7,500,000), and in fact their number never surpassed 957,000 in the ten years preceding consolidation with the Bank of the Empire and had descended in 1875 to 520,000 ($3,900,000). The maximum note circulation in 1860 was 93,029,000 thalers ($70,000,000); in 1865, 136,148,000 thalers, and 1870 202,488,000 thalers. The increase was more rapid in the next few years and carried the maximum in 1871 to 242,242,000 thalers; in 1872, to 311,531,000 thalers; in 1873 to 342,290,000 thalers; and in 1874 to 297,412,000 thalers.

The reserve of the Bank of Prussia consisted of gold and silver coin and bullion, public securities, bills of Prussian private banks, and securities payable at sight or otherwise and until 1869 of accepted drafts (*Giro-Anweisungen*). The

total of this reserve reached in 1875 about 1,900,000,000 marks ($475,000,000). The proportion of coin and bullion seldom exceeded one-third of this aggregate. The maximum in 1860 was 77,457,000 thalers ($58,000,000) and had only reached 99,427,000 thalers in 1870. The rapid increase of the number of branches of the bank scattered over Prussia and the growth of commercial operations led to an increase in the reserve during the last four years of the operations of the bank commensurate with the increase in its circulation and discounts, so that the maximum in 1874 was 239,860,000 thalers ($180,000,000) and the minimum was 203,511,000 thalers ($152,000,000). The Bank of Prussia, in spite of the share which the government enjoyed in its profits, had no monopoly of the right of note issue in the Kingdom. By its side and in competition with its numerous branches existed eight local banks, including one at Berlin, whose united capital was 8,899,000 thalers ($6,675,000) and which had the right to issue bills to the amount of 7,000,000 thalers, but in no case of a smaller denomination than ten thalers ($7.50).[1] The branches of the Bank of Prussia increased from 143 in 1867 to 158 in 1870 and 167 in 1875.[2]

The other German states were not without flourishing banks of issue, which conformed in the general features of their organization to the Bank of Prussia. There were thirty-three German banks in existence, including those of Prussia, when the Imperial Bank was established in 1875. Two of these were commercial banks and one was a territorial bank, the capital in each of these cases being furnished by the municipality or the State and the liabilities constituting a general claim against the government and the community. The others were organized as stock companies. Three of the German banks—the Bank of Bremen, founded in 1856; the Bank of Thuringia, founded in 1856; and the Bank of Anhalt-Dessau, founded in 1847—held charters without limit of time, which were regarded as perpetual. The char-

[1] Courcelle-Seneuil, 365.
[2] Noel, I., 250.

ters of the other banks ran for various periods from one year to eighty-one years. The charters of the Bank of Gera, which expired in 1953, and of the Banks of Central Germany and Lower Saxony, which expired in 1956, had been granted originally for one hundred years.

The oldest of the banks with limited charters was that of Pomerania, established at Stettin in 1821, with a capital of 6,000,000 marks. The others were: The Bavarian Bank of Mortgage and Exchange at Munich, founded in 1834; the Bank of Leipzig, in 1839; the Communal Bank of Breslau, in 1848; the Communal Bank of Chemnitz, in 1848; the Bank of United Deposits of Berlin, in 1850; the Bank of Rostock, in 1850; the Bank of Weimar, in 1853; the Bank of Gera, in 1854; the Bank of Frankfort, in 1854; the Bank of Southern Germany, at Darmstadt, in 1855; the Bank of Cologne, in 1856; the Bank of Magdeburg, in 1856; the Private Bank of Lubeck, in 1856; the Territorial Bank of Hesse, at Homburg, in 1856; the Bank of Hanover, at Hanover, in 1856; the Private Bank of Gotha, in 1856; the Bank of Central Germany, at Meiningen, in 1856; the Bank of Lower Saxony, at Buckebourg, in 1856; the Bank of Dantzig, in 1857; the Bank of Pozen, in 1857; the Bank of Brunswick, in 1857; the Commercial Bank of Lubeck, in 1865; the Bank of Saxony, at Dresden, in 1865; the Territorial Bank of Gorlitz, in 1866; the Bank of United Deposits, at Leipzig, in 1867; the Territorial Bank of Oldenburg, in 1868; the Bank of Baden, at Mannheim, in 1870; and the Bank of Wurtemburg at Stuttgard, in 1871. The Prussian banks in this list are those at Stettin, Breslau, Cologne, Gorlitz, Magdeburg, Dantzig, and Pozen, and the Bank of United Deposits at Berlin.

Many of these banks were born of the financial necessities of the governments by which they were chartered and were under obligations to aid the public Treasury. The Bank of Homburg was required to loan to the government up to a maximum of 100,000 florins ($42,000) at three per cent.; the Bank of Gotha was required to advance to the Treasury a maximum sum of 200,000 thalers ($150,000) at four per

cent.; the Bank of Bremen was required to loan a maximum of 200,000 thalers, and the Bank of Buckebourg was under obligations to make advances to the amount of 400,000 thalers without interest, on the condition that the government deposit public securities paying an interest of four per cent.[1] The State exercised a more or less complete control over all these local banks, in some cases appointing the officials and in others limiting its action to inspection and suggestion. The Banks of Bremen and Frankfort were among those enjoying comparative freedom, being subject only to public control when it was judged desirable.

The operations of these banks before 1875 consisted, like the operations of the Bank of Prussia, in the discount of commercial paper, the negotiations of foreign and domestic bills of exchange, advances upon public stocks and the precious metals and in some cases upon mortgages, and the pledge of securities and property. The building of railways, the increased productive power of the community, and the consequent increase in capital, brought a rapid extension of business to the German banks during the ten years before they become subordinate to the German Imperial Bank. The aggregate commercial discounts of all except the Bank of Prussia increased from 126,629 in number and 693,420,537 marks ($167,000,000) in amount in 1867 to 535,302 in number and 2,797,759,142 marks ($675,000,000) in amount in 1874. The management of the local state banks was for the most part prudent and conservative and they were doing a safe and profitable business when they were arrested in their growth by the policy of consolidation. Most of them had branches in the neighboring towns and cities, reaching a total of nearly fifty establishments besides the parent banks. They were required by the laws of most of the states to set aside a portion of their profits as a reserve fund and this fund increased from 12,270,712 marks ($3,000,000) in 1867 to 34,332,457 marks ($8,200,000) in 1875.

The aggregate circulation of the banks outside the Bank

[1] Noel, I., 263.

of Prussia was 181,635,305 marks ($45,000,000) in 1867, 242,502,653 marks in 1869, 432,799,730 marks in 1872 and 487,020,519 marks in 1874. The circulation of the Bank of Prussia on the latter date was 838,422,000 marks, making a total bank-note circulation for all the states of Germany of 1,325,442,519 marks ($320,000,000). The banks showing the largest circulation in 1874 were those at Dresden, 99,727,440 marks; at Mannheim, 51,901,428 marks; at Darmstadt, 46,327,015 marks; at Frankfort, 45,208,833 marks; at Leipzig, 28,464,069 marks; at Stuttgard, 25,477,028 marks; and at Meiningen, 24,000,000 marks.

The narrow limits of many of the German states and their commerce with each other led to the mutual circulation of their bills in spite of the absence of any legal tender quality even within the limits of the state where they were issued.[1] The banks of some of the smaller states took advantage of the wide circulation of their bills, and the lack of requirements for prompt redemption, by swelling their issues and by various artifices for getting the notes into circulation at distant points. Though legally redeemable in coin on demand, the small denominations of the notes and the difficulty of getting them to the counters of the issuing banks threatened to create a practically irredeemable and redundant currency, which would expel coin and bring the country to a paper basis. "They might without difficulty have remedied this abuse," says M. Courcelle-Seneuil, "by means of a system of mutual exchange and liquidation among the banks themselves, such as is practised in Scotland, and the principal banks had in their hands every power to enforce this exchange upon the banks of the small states."[2] But other means of reaching the difficulty were adopted, and the initiative was taken by Prussia, which passed an act on May 14, 1855, forbidding the circulation within her limits of for-

[1] The legal tender quality was not given by law to the notes of any of the German banks and was expressly disclaimed by the laws incorporating the banks of Pomerania, of Frankfort, of Homburg, of Meiningen, and of the United Deposits at Berlin.—Noel, I., 284.

[2] *Traité des Opérations de Banque*, 366.

eign bills payable to bearer, without interest, of a value below ten thalers. Saxony took similar action on July 8, 1855, and the small states of Thuringia concluded a convention January 21, 1856, by which they forbade the circulation of foreign bills to bearer without interest and below ten thalers in denomination, with the exception of the bank drafts of Prussia and Saxony. The Grand Duchy of Baden forbade the circulation of any foreign bills on December 24, 1855, except those issued in Prussia, Bavaria, and Nassau and at Frankfort. Prussia extended the scope of her prohibition on May 25, 1857, to all foreign bills except those below ten thalers issued by the governments of Saxony, Thuringia, and Anhalt. A Saxon ordinance of May 18, 1857, imposed a fine of fifty thalers upon the holders of foreign bills below the denomination of ten thalers except upon banks of issue which carried on a special service of exchange.[1]

The history of the circulation of these state bills outside of the limits of the issuing state suggests an interesting comparison with the circulation of the notes of the departmental banks of France and of the State banks of the United States. The banks were not in any of these cases closely linked together by clearing arrangements and the means of communication and the promptness of commercial transactions were not such as to result in the prompt return of the notes to the issuing banks for redemption. It does not appear that this resulted in a great inflation of the note issues, even in the United States,[2] but it naturally aroused fears that the banks might not be able to redeem their notes promptly on presentation and that they might fall below par

[1] Noel, I., 288.

[2] M. Wolowski, who is one of the warmest champions of monopoly of note issues, speaking of the situation in 1863, says: "Twenty banks issuing 45,000,000 thalers ($33,000,000) for thirty-two states whose population exceeded thirteen millions, is not too much as to quantity; it is too much because of the embarrassment which is caused by this diversity of monetary signs."—*La Question des Banques*, 404.

in coin. The situation in France differed from that in Germany and the United States in the respect that the notes of the departmental banks were made legal tender after the revolution of 1848 within the department where they were issued, but were forced into an inferior position by the notes of the Bank of France, which were legal tender throughout the republic. The circulation of the bank-notes of Germany and the United States without the legal tender quality might have been maintained at par with coin (from which they do not seem to have departed in Germany) under a system of closer union among the banks and prompter means of communication.

The government of Prussia took action as early as 1846 towards the centralization of the banking system, by the ordinance of October 5th, which provided that the provincial banks of the Kingdom should cease their operations when the Bank of Prussia should lose its special privileges. Another act, which indicated the purpose of the government to keep matters in its own hands, was the law of May 7, 1856, renewing the privileges of the Bank of Prussia, but reserving to the executive power the right at the end of 1871 and every ten years thereafter to dissolve the bank and return the capital to the shareholders. This provision necessarily exposed the other banks, under the ordinance of 1846, to dissolution as banks of issue at the end of the same period. The law remained in this condition until the reorganization of the North German Confederation under the headship of Prussia in 1867. A provision was then incorporated in the constitution of North Germany confiding to the Federal Assembly exclusively the regulation of banks of issue. The power remained in abeyance for a few years, when the law of March 27, 1870, reserved to the Confederation the right of granting the power of issue or of increasing the monetary circulation. The law stipulated that the renewal of the privilege of issue should not henceforth be granted except upon the condition that it might be revoked at any time upon preliminary notice of one year. It was also provided that where a bank possessed the right of issue for a definite

term, subject to preliminary notice of withdrawal, this notice should be regarded as having been given.

The monetary system of Germany called for radical reform, without regard to the banking policy adopted, in order to facilitate exchanges among the German states and with foreign countries. The coins were of such different denominations and degrees of abrasion that heavy exchange charges were levied on the borders of every little state and possible profits on merchandise were almost neutralized by this loss. Several conventions to simplify the monetary system were held before the unification of the Empire, one of the latest at Vienna on January 24, 1857. The basis of an agreement was then prepared abrogating the old systems and adopting one based upon the new pound of five hundred grams which was in use in several continental countries. Germany was divided by this convention into three zones. Silver was treated as the single standard of value and was to be coined into two forms,—the thaler, equivalent to a florin and three-quarters, and the florin, worth four-sevenths of a thaler. It was proposed to coin thirty thalers out of a pound of five hundred grams of fine silver for use in the Northern States and fifty-two and a half florins out of a pound for use in the South. Other silver pieces of one and two thalers were to be coined with special devices, under the name of the union thaler (*Vereinthaler*), for trade between North and South Germany, and were to be received by public depositories as lawful money.

Silver constituted the principal metallic stock of Germany and of the cash resources of the local banks up to the time of the monetary reform. Gold figured somewhat in the circulation, but it was not a legal tender.[1] The gold pieces, coined under the convention of 1857 according to mint re-

[1] Mr. Shaw declares that the convention in 1857 had a part of its motive in the wish by the German States "to protect that part of their currency system which was threatened by bimetalic law," and that France drew gold from Germany as well as from California and Australia as the result of the change in the ratio.—*History of Currency*, 205-11.

gulations, were to be received at a valuation in standard silver money known as "the bank rate," which was fixed in advance for six months and was never to be higher than the mean quotations in the market. The character of the circulating medium was further complicated by a circulation of government paper money, which was issued by every German state except the principality of Lippe and the three free cities of Hamburg, Bremen, and Lubeck. The adoption of the gold standard was first formally recommended by a commercial convention of one hundred and nineteen German cities which sat at Berlin between October 20, and October 23, 1868.[1] A resolution was presented by Dr. Adolph Soetbeer, who was the official reporter on the subject of the standard at an earlier session held in September, 1865, declaring that "a monetary unity, and at the same time such a general monetary reform as befits the age, can be brought about by the adoption simultaneously by all the German States of the single standard with full application of the decimal system, in pursuance of the principles recommended by the International Monetary Conference of Paris in its report of July 6, 1867." This resolution was adopted, including the recommendation of a unit of value equivalent to the gold five-franc piece, and the public authorities were recommended to put it in force not later than January 1, 1872, when the new system of weights and measures already adopted by the North German Confederation took effect.[2]

The payment of the great war indemnity by France gave Germany the opportunity to carry out the recommendations of her leading economists, that she adopt the gold standard. The direct payments in French gold were only 273,003,058 francs ($52,600,000), but the power given the German government to draw the proceeds of bills of exchange upon London and Paris gave them access in a large measure to the

[1] Appendix to American Report on International Monetary Conference of 1878, Sen. Ex. Doc. 58, 45th Congress, Third Ses., 727.

[2] M. Allard, the honorary director of the Belgian mint, declares that silver was "academically demonetized" by the vote of the Paris Conference.—*La Crise Agricole et Monétaire*, 41.

gold of the world. The German government kept an account with the London Joint-Stock Bank which was believed to run as high as £4,000,000 ($20,000,000)[1] and by watching the market were able to rapidly carry gold into Germany. The law establishing a uniform coinage (Act of December 4, 1871) did not adopt the five-franc piece as the unit, as recommended by the convention of 1868, but adopted a unit called the mark, equivalent to one-third of a Prussian thaler, and established the ratio of fifteen and a half to one between gold and silver. The provision of the treaty of Vienna, providing for the coinage of the union thaler of silver, was repealed. Gold legal tender coins were provided for, but the Imperial gold standard was not fully established until the coinage act of July 9, 1873, when it superseded all local standards and made the monetary unit the mark of gold.[2] The Imperial silver coinage was to be carried on on government account, and limited to ten marks per capita, and was to be a legal tender for only twenty marks between individuals, but payable in any sum to the government. The new silver coins were made mere token coins, by reducing the weight of the fine silver eleven and one-ninth per cent. below the full weight at the ratio of fifteen and a half to one and coining a pound of fine silver into one hundred marks and a pound of fine gold into 1395 marks.

One of the interesting incidental results of the new coinage laws was the termination of the career of the old Bank of Hamburg, which had for more than two and a half centuries been carried on on the principles of the Bank of Venice and the Bank of Amsterdam. The accounts of the bank were kept in marks banco, representing a bank credit of the uniform value of half a thaler (37½ cents), and its notes were redeemable in silver. The Bank of Hamburg, founded in 1619, was the last survivor of the medieval banks, created

[1] Bagehot, *Lombard Street*, Works, V., 199-202.

[2] The exact equivalent of the mark in American gold coin is twenty-three and eight-tenths cents, but for convenience of computation in dealing with large figures it is treated in this work as substantially equal to a quarter of a dollar.

for the purposes of foreign commerce. Accounts could be opened only by a Hamburg citizen or corporation and were transferred only upon his appearance in person or by attorney with a transfer order. The principle upon which the bank was conducted was the granting of a credit on the books for the silver or gold deposited. No loans were made and no notes or other liabilities were created beyond the amount of coin and bullion on deposit. So faithfully was this rule adhered to that when the French on November 5, 1813, took possession of the bank they found 7,506,956 marks in silver held against liabilities of 7,489,343 marks. They removed a large part of the treasure before the freedom of Hamburg was re-established on June 1, 1814, but the bank resumed business with unimpaired credit and the thefts of Napoleon's forces were made good in 1816 by a transfer of French securities. Modern banking methods were gradually introduced into the Bank of Hamburg and a capital was accumulated of about 1,000,000 marks ($250,000) in addition to the buildings. The bank survived the storm of the crisis of 1857, only to fall under the decrees establishing the new German monetary system, which ordered the bank to liquidate its accounts in fine silver by February 15, 1873. The latest reference to its existence is found in the proceedings of the Hamburg Senate on October 13, 1875, declaring their purpose to sell to the Bank of Germany for 900,000 marks the buildings of "the venerable institution which had performed such great services to German trade."[1]

The accumulation of a stock of gold was begun by the Imperial Bank and the government, and the purchases of gold by the bank, from January 1, 1876, to the end of 1893, amounted in American money to $434,890,067. The coinage of Imperial gold coins from 1872 to the close of 1893 reached 2,737,790,915 marks and the aggregate coinage of silver 484,048,609 marks. The sales of silver by the government up to March 31, 1893, represented a coining value of 672,862,729 marks, but the amount actually received was

[1] Palgrave, *Dictionary of Political Economy*, I., 105.

574,055,532 marks, showing a loss of 98,807,197 marks.[1] The bulk of the sales were made before May 16, 1878, before the great decline in the price of silver, and the highest price per kilogram was obtained in the period of the largest sales, between September 30, 1876, and September 30, 1877.[2] The profit on the gold, silver, and subsidiary coinage, taking these coins at their face value, was 96,380,330 marks, and the cost of recoinage added to the loss on silver was 127,894,218 marks, showing a net loss of 31,513,888 marks.

The banking system of the Empire was unified in a measure by the provisions of the law of July 9, 1873, that bank bills should be withdrawn from circulation before January 1, 1876, if their value was not declared in Imperial marks, and that the smallest notes should be for 100 marks ($23.80). The work of unification was completed, so far as it was possible to complete it, by the Imperial law of March 14, 1875, which was supplemented by the Prussian law of March 27th and a convention between Prussia and the Empire on May 17th and 18th following. The Royal Bank of Prussia was directed to cease its operations on December 31, 1875, and to transfer its rights and privileges to a new bank, known as the Bank of the Empire (*Reichsbank*). The government of Prussia was allowed to withdraw its capital of 1,906,800 thalers in the old institution and the half of the reserve fund belonging to it. The Prussian government was further compensated for the surrender of its rights in the bank by an indemnity of 15,000,000 marks ($3,750,000), paid from the Treasury of the Empire, and a pledge that

[1] The equivalent for these sums in American money, as given in the American translation of the Report of the Berlin Silver Commission of 1894, are: Gold coinage, $651,594,221; silver coinage, $115,203,549; face value of silver coins sold, $160,141,329; price received, $136,625,216; loss on sales, $23,516,113; net loss after deducting profits, $7,500,308.—Sen. Mis. Doc. 274, pt. I., Fifty-third Congress, Second Session, 33-36.

[2] The sales during this period were not far short of half of the whole, being 1680.4 kilograms and representing a face value of 302,500,000 marks. The average price of silver in 1876 was $1.156 per ounce and in 1877, $1.201 per ounce.

the new bank should continue the annual payment of 621,910 thalers ($465,000) from 1876 to 1925 which had been agreed upon by the Bank of Prussia in 1856.[1] The Imperial government agreed to be responsible for this annuity in case the privileges of the bank were not continued. The shareholders of the Bank of Prussia were given the option of receiving back their capital in cash, in accordance with the pledge of the Prussian law of October 5, 1846, or receiving shares of equal face value with their existing holdings in the new Imperial Bank. The new bank on these conditions succeeded to all the rights and obligations of the Bank of Prussia. The Chancellor of the Empire was authorized to acquire the bank shares which should be exchanged for the shares of the Bank of Prussia and to issue interest-bearing Treasury bonds maturing not later than May 1, 1876, to the amount of the shares not issued, in order to complete the capital of the new institution. The capital was fixed by law at 120,000,000 marks and was divided into 40,000 shares of 3000 marks ($750) each, of which 19,919 shares replaced the shares of the Bank of Prussia which the holders had chosen to convert; 20,000 shares were placed by public subscription, and 81 by means of sales on the Bourse.

The organization of the Imperial Bank made it entirely a private institution as to ownership, but essentially a public one in its management. "In fact," says M. Octave Noel, "the establishment is closely bound to the state and is only able to move, think or act when the state manifests in some manner its presence and affirms its control." The official control over the bank is confided to a council of curators, composed of the Chancellor of the Empire, who is President, and four other members, one named by the Emperor and the other three by the Federal Council. The direction of the policy of the bank is so completely under the orders of the Chancellor that in case of his absence or impeachment the presidency of the Council is vested temporarily in an official named by the Emperor. The Chancellor or his substitute

[1] Noel, I., 248.

directs the entire administration and issues the instructions to the council of direction, to the branches and to the employees of the bank. The committee of curators meet every three months and examine reports regarding the bank's condition and the operations which are being carried on. The administrative authority is vested in a directorate composed of a president and a number of members named for life by the Imperial government upon the nomination of the Federal Council. The official force of the bank, although paid from the funds of the institution, are subject to the same obligations and enjoy the same privileges as the public employees of the Empire. Honors and pensions are accorded them, benefits are voted to the families of deceased employees, the number of posts and the salaries are included in the Imperial budget, and the accounts are subject to the control of the accounting officers of the Empire. The employees of the bank, moreover, are forbidden by law to hold stock in the institution.

The influence of the private owners is exerted through a central commission of fifteen members and fifteen alternates, elected by the general assembly of the shareholders from their own numbers. These commissioners are required to possess in their own right not less than three shares, to have their domicile within the Empire, and nine members and nine alternates are required to be residents of Berlin. A third of the board is elected every year and the members are eligible for re-election. Many of the business details of the management of the bank are remitted to this central commission, so long as their course does not meet the disapproval of the Imperial authorities. They are required to examine every three months the weekly reports, to inspect the deposit accounts, and to determine what proportion of the bank funds shall be used in advances and in the purchase of paper, what the rate of discount shall be, and what arrangements shall be made with other German banks. A still smaller body of three members of the central commission is charged with the daily supervision of the bank's af-

fairs and they are authorized to sit at all meetings of the directorate with consulting powers.

The note circulation of the Imperial Bank is based largely upon the English banking act of 1844, but with an important modification which adds greatly to the ability of the bank to provide accommodation in times of stringency. There is a fixed limit of authorized circulation, against which cash or its equivalent must be held in the proportion of one-third, and issues beyond this limit must be covered in cash for the full amount. The cash reserve of one-third in the one case and one hundred per cent. in the other may consist of money having currency in Germany, Imperial Treasury bonds, gold bullion, or foreign gold coin. The notes, therefore, are issued against the general assets of the bank, which remain wholly within its own control and are not set aside by specific designation or prior lien for the security of the note holders. The law, says Prof. Dunbar, "has simply provided by suitable measures that the affairs of the bank, including its issue of notes and the money and securities held by it, shall meet certain tests of soundness, believing that both the ultimate solvency of the bank and the prompt payment of its circulation are thus made secure."[1] The limit of authorized circulation was fixed by the law of March 14, 1875, at 250,000,000 marks ($60,000,000) but the same law provided that when any existing bank of circulation should surrender its right, either by liquidation or by refusal to accept the conditions imposed by the new law, the amount of the circulation might be assumed by the Imperial Bank. Seventeen banks surrendered their right to issue notes soon after the adoption of the new system and their action added 26,085,000 marks to the authorized circulation of the Imperial Bank. This has since been increased to 42,117,000 marks.[2] The two-thirds of the authorized circulation not covered by the cash reserve are required to be covered by

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[1] *Theory and History of Banking*, 195.

[2] Raffalovich, *Marché Financier en 1893–4*, 67.

bills of exchange maturing in not more than three months and bearing not less than two solvent names.

The novel feature of the German system of circulation is the authority given to the Imperial Bank to exceed the statutory limit of note issue without metallic security, upon the payment of a tax at the rate of five per cent. per year upon the excess of circulation. Weekly reports are required by the government and upon the excess of circulation shown above the limit a tax of $\frac{5}{360}$ per cent. is at once assessed, representing approximately the tax for a single week at the rate of five per cent. a year. This provision permits increased issues when there is stringency enough in the money market to carry current discount rates above five per cent. but drives the new notes promptly out of circulation when the discount rate falls. The operation of the rule, which has been several times availed of by the Imperial Bank and by other German banks, has proved salutary in averting such stringency as has been felt in England under the Act of 1844, while it has kept the circulation within the limits set by the needs of business.

The first issues of the Imperial Bank subject to the five per cent. tax occurred in December, 1881, and were repeated in September and October, 1882; in December, 1886; and three times in the latter part of 1889, when the excess above the limit ran as high as 109,473,000 marks ($26,000,000). The limit was exceeded in 1890 by 26,250,000 marks ($6,500,000), but at the end of 1891 the reserve had been so increased that the note issues were 101,407,000 marks below the limit. This margin was reduced to 16,764,000 marks ($4,000,000) at the end of 1892, and the bank was compelled in February, 1893, to pass the limit, to maintain an excess of circulation until March 30th, and to avail itself again of the privilege of passing the limit on May 23d. The bank was 8,000,000 marks within the limit at the end of the year and 123,000,000 marks within it at the end of 1894. The occasion of the high interest rates and the demand for money in 1893 was the withdrawal of deposits from Berlin by the Russian government, the effort of Austria-Hungary to restore specie

payments, the heavy offerings of Italian bonds and the important financial events in India, Australia, and the United States.[1] The years 1894 and 1895 passed without any excess of the circulation above the limit.

The rate of discount charged by the Imperial Bank has averaged 4.04 per cent. since its organization on January 1, 1876. The variations have not exceeded seven in any one year and have usually been fewer. The mean from 1876 to 1881 was 4.42 per cent. ; from 1882 to 1887, 4.57 per cent. ; and from 1889 to 1893, 3.82 per cent. The mean rates for the past six years have been 4.51 in 1890 ; 3.78 in 1891 ; 3.20 in 1892 ; 4.06 in 1893 ; 3.11 in 1894 ; and 3.16 in 1895. The rate in 1893 was permanently higher than for a long period. It began at four per cent., and was reduced on January 17th to three per cent., but was advanced on May 12th to four per cent. and on August 11th to five per cent., where it remained until January 9, 1894. It was then reduced to four per cent., and on February 5th to three per cent.,[2] where it remained until November, 1895, when it was advanced to four per cent.

The local banks of Germany were brought by the law of 1875 under the same rules as the Imperial Bank and drastic regulations were enforced to compel them to comply with the new law or abandon the issue of circulating notes. The purpose of the new legislation, to bring the control of the bank-note circulation as soon as practicable into the hands of the Imperial Bank, was indicated by the declaration that the power to issue bank-notes or to increase circulation beyond the limit already authorized by the various states should be granted only by a law of the Empire. Prussia was almost supreme in the Federal Council and there was little likelihood that she would consent to any law increasing the circulation of the local banks. The long duration of the privilege accorded to some of them was cut off by a provision that their privileges should be subject to revocation on January 1, 1891,

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[1] Raffalovich, *Marché Financier en 1893–4*, 62–63.
[2] Raffalovich, *Marché Financier en 1894–5*, 112.

and every tenth year thereafter, upon one year's notice and without indemnity, if they accepted the power of note issue involved in the new law. Those banks which were not disposed to accept the new conditions were dealt with in a manner similar to the departmental banks of France after the revolution of 1848. They were not deprived of the privilege of issuing notes, but they were forbidden by Article 42 of the law to carry on banking operations, outside the limits of the state which had given them the privilege, by means of branches or agents or to hold shares in other banks. Another provision (Article 43) declared that "The notes of banks having the privilege of note issue at the time of the promulgation of this law, shall not be employed in payments outside the state which may have granted them the privilege. The exchange of these notes, however, for other bank-notes, paper money, or specie is not subject to this prohibition."

Banks which saw fit to submit to the new conditions were treated somewhat more favorably, pending the extension of the branches of the Imperial Bank throughout the Empire. They were governed by Article 44 of the law and were subject to the same conditions, as to the classes of securities dealt in, the character of the commercial paper held, the proportion of cash reserve to circulation and the payment of benefits to the state, as the Imperial Bank. They were required to hold security for their circulation to the amount of one-third in money having currency in Germany, in Imperial Treasury bonds, in gold bullion or foreign gold coin. The remaining two-thirds of the circulation was required to be protected by bills of exchange running for not more than three months and bearing three endorsements or not less than two names of well-known solvency. They were required to exchange their notes for German money having currency at Berlin, or Frankfort, and redemption must not be delayed beyond the morrow of the presentation of the note.[1] Banks accepting these conditions obligated themselves to receive at their face value, in branches established in cities of more

[1] Noel, I., 320–23.

than eighty thousand inhabitants and at the parent bank the notes of German banks whose circulation was authorized throughout the Empire and which were redeemable in coin on demand. Bills on one bank thus received by another could be used only in the settlement of balances with the bank of issue, employed in payments within the territory of the issuing bank or presented for redemption. Banks desiring to conform to the requirements of Article 44 were required to present to the Chancellor of the Empire the evidence that their statutes conformed to the law and that the locality chosen for the exchange of bills (Berlin or Frankfort) possessed a branch ready for actual operation.

Much feeling was aroused among the German banks upon the passage of this law and fifteen of the thirty-two outside the Bank of Prussia promptly abandoned their right to circulation, and became mere private banks of discount and deposit, rather than conform to all the requirements of the new law. The Bank of Brunswick took the bolder course, which it was believed no bank would be able to maintain, of refusing to comply with Article 44 and continuing its circulation under the limitations of Articles 42 and 43. The Bank of Brunswick, therefore, continued to issue bills which circulated within the limits of the duchy and braved the efforts of the Bank of Prussia to force it into submission. The Prussian Bank refused to receive the paper of the Bank of Brunswick and upon the failure of this device had orders issued to the postal savings banks not to receive the notes of the bank on deposit. The latter measure threatened to arouse so much of the old separatist feeling in Germany that it was abandoned by direction of the Chancellor. Frederick William of Brunswick died during the latter part of 1884, and Prince Albert of Prussia, the nephew of the German Emperor, was elected Duke of Brunswick by the Diet on October 21, 1885. The close relations thus established between Brunswick and the Imperial government soon led to the compliance of the Bank of Brunswick with the provisions of Article 44.

The purpose to clear the field for the circulation of the Im-

perial Bank was indicated by a law of April 30, 1874, which required the retirement of the paper money issued by the various states not later than July 1, 1875. The Imperial government, in order to promote this policy, was authorized to issue Treasury bonds to the amount of 120,000,000 marks ($30,000,000) and to apportion them among the states according to population. The paper money in circulation was 61,374,599 thalers ($45,000,000), and it was not distributed in any such even ratio as the new bonds. The law, in contemplation of this situation, authorized the Imperial Treasury to advance to states which needed an additional allowance to retire their paper money a sum in Treasury bonds equal to two-thirds of the excess of notes above the original apportionment of bonds. These bonds were to be receivable by the Imperial Treasury and were to be convertible on demand into metallic money. The advances of bonds in addition to the apportionment of 120,000,000 marks, were 54,919,941 marks, of which Saxony received 19,013,441 marks; Bavaria, 14,534,975 marks; Baden, 4,577,449 marks; Wurtemberg, 3,309,651 marks; Hesse, 3,250,514 marks; and the other states less than 2,000,000 marks each. Prussia received no additional advance, but her share of the original allotment was 72,145,494 marks. Oldenburg, Lippe, Lubeck, Bremen, Hamburg, and Alsace-Lorraine received no extra advance.

The sixteen banks which decided in 1875 to accept the federal regulation of their circulation and to continue to issue notes were, besides the Imperial Bank and the Bank of Brunswick, the Municipal Bank of Breslau, and the banks of Magdeburg, Dantzig, the Grand Duchy of Posen, Hanover, Frankfort, Bavaria, Saxony, United Deposits at Leipzig, Chemnitz, Wurtemberg, Baden, Southern Germany, and Bremen. Provision was made in the new law for a new bank in Bavaria, with which two existing banks were consolidated, and which was given special permission to issue circulating notes to the amount of 70,000,000 marks. The authorized uncovered circulation of these sixteen banks was 111,125,000 marks, of which the Bank of Bavaria was

originally entitled to 32,000,000 marks, the Bank of Saxony at Dresden to 16,771,000 marks, the banks of Frankfort, Baden, Wurtemberg, and of Southern Germany to 10,000,000 marks each, and the others to smaller amounts. The absorption of the issues of these banks by the Imperial Bank has proceeded rapidly in recent years. Only eight banks of circulation remained in existence in Germany at the close of 1891, outside the Imperial Bank. They included the larger of the banks named above, and their aggregate capital was 130,000,000 marks ($32,000,000). The circulation of the local banks fell from 200,300,000 marks ($50,000,000) in 1883 to 192,400,000 marks in 1890, but their metallic reserve increased from 111,200,000 marks to 112,600,000 marks.[1] Two more banks surrendered their issues within the next four years and at the beginning of 1896 the six banks of circulation remaining, with the limit of their issues, were as follows: Baden Bank, 27,000,000 marks; Bank of Southern Germany, 36,981,000 marks; Bavarian Bank, 70,000,000 marks; Brunswick Bank, 10,500,000 marks; Frankfort Bank, 34,285,700 marks; Wurtemberg Bank, 25,714,200 marks.[2]

The principal items in the accounts of the Imperial Bank since its creation are shown in the following table:

YEAR.	MEAN CIRCULATION.	MEAN METALLIC RESERVE.	MEAN DISCOUNTS.	MEAN ADVANCES.	MEAN CURRENT ACCOUNTS.
	(In millions of marks).				
1876	684.8	510.5	——	50.9	70.5
1878	622.6	494.0	340.8	52.4	109.9
1880	735.0	562.0	345.7	51.3	124.9
1882	747.0	548.9	372.1	54.4	111.9
1884	732.9	591.7	377.7	49.1	155.2
1885	727.4	586.1	372.7	52.4	162.4
1888	933.0	904.0	430.0	52.0	247.0
1890	942.0	801.0	543.0	98.0	248.0
1891	971.0	890.0	546.0	98.0	360.0
1892	984.0	962.0	541.0	95.0	463.0
1893	984.0	824.0	581.0	85.0	513.0
1894	1,000.0	934.0	548.0	81.0	491.0
1895[3]	1,320.0	853.0	880.0	100.2	439.5

[1] *Bulletin de Statistique*, Nov., 1891, xxx., 542.

[2] Comptroller's Report, 1895, Report of Minister Runyon, 830.

[3] Actual condition December 31st.

The proportion of the metallic reserve which is in gold is not regularly reported, but was stated in a government report of May 10, 1892, at 624,977,000 marks ($150,000,000). The amount at the end of 1894 was 714,448,000 marks ($170,000,000), and is now estimated at 750,000,000 marks ($180,000,000). The circulation of specie in all small transactions in Germany is ensured by the limitation of the minimum value of the bank-note to one hundred marks ($23.80). The act of July 9, 1873, required all the German banks to withdraw from circulation bills below this value as well as those which were not expressed in Imperial marks. Redemption in coin on demand is required at the Imperial Bank in Berlin, but may be refused at the branches when the funds on hand do not justify it. The bank is obliged to receive the bills of other banks of issue which have conformed to the law of March 24, 1875, and where they are established in cities of more than 80,000 inhabitants. Bank bills are not a legal tender, however, between individuals, and the law prescribes that "there exists no obligation to accept bank bills for payments which are legally due in specie, and no such obligation can be established by the legislation of any state with regard to the banks of the state."

The government took advantage of the extension of the charter of the Imperial Bank in 1889 to secure a larger share in the dividends than it had before demanded. The statute of December 18, 1889, reduced from four and a half to three and a half per cent. the dividend allotted to the shareholders before any other allotment. Twenty per cent. of the remaining profits was to be carried to a reserve fund, so long as this fund was less than a quarter of the capital, and the remainder was to be shared equally between the shareholders and the Imperial Treasury until the portion of the shareholders reached six per cent. Of the profits in excess of six per cent. the shareholders obtain only a quarter and the Imperial Treasury the other three-quarters. The minimum dividend of three and a half per cent. was to be made up to the shareholders from the reserve funds when it was not provided by the annual profits of the bank. The reserve

fund reached the legal limit of one-fourth of the capital in 1891. The old law divided the dividends above four and a half per cent. equally between the shareholders and the government up to eight per cent. The actual profits under the old law from 1876 to 1888 were 131,900,000 marks, amounting to 8.46 per cent. annually on the capital. The shareholders received 94,900,000 marks, amounting to 6.08 per cent. of the capital and the state received 24,700,000 marks. The bank had at the beginning of 1895 267 banking offices and 1745 employees, and the cost of administration during 1894 was 9,069,380 marks ($2,250,000). The dividend declared for 1894 was 6.26 per cent. to the 7877 shareholders and more than half as much to the government.

The Imperial Bank has done much of late years to assist the cultivators and small tradesmen, but not all that the German socialists desire. The president recently had occasion to remind them that the bank was not in a position to accord long credits and that this condition was expressed in the fundamental law, forbidding the discount of paper for more than four months. "Within the limits of its statutes," said he "the bank accords to small but sound customers a suitable credit, when and so far as their conduct and fortune offer guarantees of the punctual fulfilment of their engagements. Artisans and merchants less fortunate are always able to unite with advantage in a credit association."[1] This suggestion has long since been acted on in Germany through the Schulze-Delitzsch associations. These are co-operative popular banks whose members comprise the smallest artisans, domestics, and shop-keepers. They form, says Professor Jannet, "a hierarchy of banks which by the successive rediscount of their paper cause the bills of exchange of the most modest artisans to reach the Imperial Bank."[2]

[1] Raffalovich, *Marché Financier en 1894–5*, 116.

[2] *Le Capital, la Spéculation et la Finance*, 563. Mr. Henry F. Merritt, the efficient United States Consul at Barmen, indicates that the Imperial Bank even makes loans to associations not doing a strictly short term business, but states that at the general meeting of the *Neuwieder Centralskasse* at Mainzon on June 20, 1894, com-

President Koch stated at the annual meeting in 1895 that 54,641 persons or firms were admitted to discount at the bank during 1894, of whom 6414 were agriculturalists. From April 1, 1893, to April 1, 1894, the bank had purchased 216,000,000 marks of bills bearing agricultural signatures, besides discounting directly 24,000,000 marks more. The associations having connections with the bank, he declared, contained 502,451 members, of whom 127,229 belonged to the rural associations, and they had at their disposal 60,000,000 marks of the funds of the bank.

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plaints were made that the Imperial Bank would only advance them money at five and a half per cent.—*U. S. Consular Reports*, December, 1895, 18.

CHAPTER IX.

THE AUSTRO-HUNGARIAN BANK.

The Evils of a Century of Paper Money—The First Issues of Notes and the Efforts to Restore Coin Redemption—The Creation of the Imperial Bank and the Successive Changes in its Charter—Establishment and Growth of the Hungarian Branch—The Monetary Reform of 1892 and the New Rate of Exchange—Use of Certificates of Deposit.

THE Austrian Empire has been for a century under the dominion of paper money, but her monetary history has differed from that of France with the *assignats* and the United States with the Continental money of the Revolution. The Austrian paper money has been a serious detriment to the commercial development of the country and the solidity of business enterprises, but the volume has never reached the point of absolute worthlessness and repudiation. The effect of the system has been, in the language of Professor Sumner,[1] "not like an acute disease; it is like an invalid state with occasional fever." The first issues of paper money seem to have had the same beneficial effects as the issues of Law's bank in France and the issues of £1 bank-notes in Scotland, in stimulating business enterprises and affording a convenient circulating medium where none existed, but the limit was soon over-passed and the Austrian paper money began its downward course. This course has been several times arrested by earnest efforts on the part of the government, only to be resumed when the necessities of war compelled new issues of paper. The fi-

[1] *History of American Currency*, p. 323.

nancial history of the Austrian Empire has been a succession of acts for refunding, for new issues of interest-bearing and non-interest bearing securities, and new regulations for the Austrian National Bank until the recital becomes almost tedious. The government and the bank have been able in recent years to accumulate a large stock of gold, the paper money has risen much above the value of standard silver coins, and unless the country is dragged into some new war she will soon accomplish the resumption of specie payments upon a gold basis.

The first important banking institution in Austria seems to have been created at Vienna by a decree of June 16, 1703, with a capital of 7,000,000 florins ($3,500,000). It was created for the purpose of rescuing the government from the evils of a debased currency which even then existed, but was authorized to receive the deposits of individuals, like the similar establishments of Venice, Hamburg, and Amsterdam. It was essentially a governmental institution and was formed, like the Bank of Venice, for the funding of the public debt, which was to be accomplished by an annual levy upon the receipts of the Treasury for the security and retirement of the mandates or *assegni* which the new establishment was authorized to issue.[1] The experiment was not successful. The government was unable in the involved state of the finances to make the annual payments to which it was pledged and the mandates issued by the bank were received very reluctantly into the monetary circulation. The government finally turned the institution over to the City of Vienna and it took the name of the Bank of the City of Vienna. The transformation did not save it. The bank suspended operations in drafts on private account in order to devote its entire resources to refunding, but the expected means for this work failed and the bank went into liquidation at the expense of its depositors and shareholders. No further attempt was made to establish a national bank for over a century.

[1] Noel, I., 344.

The Austrian Empire found itself in 1761 in one of the most critical stages of its history. The headship of Germany, which descended to the Hapsburgs from Charlemagne, was escaping from Austrian control under the potent influence of Frederick the Great of Prussia, and Austrian finances were involved in an inextricable confusion in which the one patent fact of a deficit was all that was not obscure. The Count of Sinzendorff, one of the leading ministers of the Empire, noticed that the condition under which loans were contracted afforded no opportunity to small capitalists to invest. He presented, therefore, a project by which bills of from 20 to 100 florins were issued, with coupons attached indicating the value from day to day, with interest added at six per cent. Public depositories were authorized to receive these bills in payment of taxes and to disburse them to the creditors of the State at their value at the date of payment, including accrued interest. M. Noel says regarding the effects of this issue :

> The public were not slow to receive these bills with favor and the circulation attained immediately such proportions that the government felt able to dispense with the provision for interest, which created a heavy charge upon the Treasury. It decided to substitute, by a system of exchanges from day to day, paper money without interest for the original interest-bearing bills, which represented a particular kind of Treasury bonds; and in redeeming the last, in order to avoid confusion, it issued notes of five, ten, twenty-five, fifty, and one hundred florins. Public opinion showed itself as favorable to the employment of the new money as to the circulation of the first, and the numerous facilities which it gave to daily transactions gave it a preference even over metallic money.[1]

The government could not content themselves with the moderate use of the power in their hands. A second issue of notes was decreed in 1769 and a third in 1771. Commerce was expanding, aided to some extent by the convenience of the new note issues, and the government seized the opportunity for injecting fresh masses of paper into the circulation. These excessive issues provoked a panic in 1797, which

[1] *Banques d'Émission en Europe*, I., 340.

obliged the government to give forced legal tender character to the paper and even to refuse its conversion into securities of the consolidated debt. Specie rose to a premium of thirteen per cent. in December, 1799, and began to disappear from circulation, and in 1800 the Treasury attempted to fill its place by the creation of notes of one and two florins (fifty cents and one dollar). Austria lost several Italian provinces as the result of the brilliant campaigns of Napoleon, and the inhabitants of those provinces who held Treasury bills overran the public depositories with the demand for payment in specie. The separation between coin and paper constantly grew wider, until in 1806 paper circulated for only half its value in silver, which was then the metallic standard. The Treasury made repeated promises, which could not be kept, that a part of the annual tax levy should be consecrated to the reduction of the paper circulation. The need for funds was so urgent that decrees were issued ordering the transmission to the Treasury of silver vessels, jewelry, the decorations of the churches and the consecrated fonts throughout the empire, which were paid for in paper money at three times their specie value.

The peace which followed the French victory at Wagram in 1809 and the marriage of the Archduchess Maria Louisa with Napoleon afforded an opportunity, which the government embraced, to attempt the restoration of order in the public finances. Delegates from all the provinces were assembled, but they found almost insuperable difficulties in the inefficiency and corruption of public officials and the absolute lack of confidence by the business community and the people in the oft-broken pledges of the government. The issues of government paper money had steadily increased from 74,200,000 florins ($37,000,000) in 1797 to 1,064,000,000 florins ($530,000,000) in 1811. The value of the paper had declined almost in proportion to the increase in the issues. The price of silver expressed in paper was 118 in December, 1800. It steadily rose to 203 in 1807, leaped to 500 in December, 1810, with the enormously increased issues of the three intervening years, and touched 1200 for a time in 1811.

The method adopted in France, when the territorial mandates were substituted for the *assignats*, was followed by Austria, which declared the reduction of existing issues to one-fifth of their original value and substituted redemption notes (*Einlosungsscheine*), which were called Viennese money. The decree of February 20, 1811, which put this reduction in force, was issued with the avowed purpose of arresting the fluctuations in the paper money, which were declared to be "so extremely pernicious, because they shatter private fortunes, fetter industry, derange all social relations, and give birth to distrust and jealousy."[1] The decree was despatched under seal to the officials in different parts of the Empire, to be opened at five o'clock in the morning on March 15, 1811, and the announcement was awaited by eager crowds who looked to the action of the Emperor to relieve the public distress. The majority, who held quantities of the paper, went away cursing the government for the decree. A few, who were believed to have had previous notice of its contents, had put their affairs in a shape which left them rich, as some of the purchasers of stock in the Mississippi Company of John Law had transformed it into real estate or exported the proceeds in coin while the stock was still selling at high figures. The government promised to limit the new issues of redemption paper to just enough to redeem the outstanding notes in the proposed ratio of one to five, which would be about 212,000,000 florins. The new notes were depreciated, however, from the first day of their issue and fell to fifty per cent. during the year, but rose to eighty-seven per cent. when the public began to believe that the quantity would not be increased. The suspension of new issues was only for a brief period and the necessities of the last Napoleonic wars forced the issues up to 638,900,000 florins ($319,000,000) in 1816.

The distrust and business paralysis caused by these repeated paper issues and the necessity of raising money to carry on the government led to the creation of the National

[1] Leroy-Beaulieu, II., 644.

Bank of Austria. The Emperor, in issuing the imperial patent for the establishment of the bank, invoked the public confidence by declaring that he had from the first desired to re-establish order in the standard of value, but that the violent shocks which had rent Europe asunder had involved Austria in a series of difficult wars, in which the preservation and the independence of the monarchy became dearer than mere questions of finance. He pledged himself to the people that no new paper money should be put in circulation and that the withdrawal of that already out should be confided to a national privileged establishment.[1]

A party of capitalists was formed after some delay and the statutes of the National Bank of Austria received the Imperial approval on July 15, 1817. The bank was accorded for twenty-five years the exclusive privilege of note issues, was exempted from the stamp taxes, and was authorized to accept deposits and discount commercial paper. The entire capital was to be 110,000,000 florins ($55,000,000) in shares of 1100 florins each, payable 100 florins in silver and 1000 florins in paper. The bank was able to dispose of only 50,621 shares, from which the proceeds were $2,600,000 in silver coin and $29,000,000 in paper. The government took up and destroyed the paper and issued an equal amount of securities bearing interest at the rate of two and a half per cent. As the notes were depreciated to one-third of their nominal value, this amounted to seven and a half per cent. upon the real capital realized, which was about $12,300,000 ($2,600,000 in coin and $9,700,000 in the coin value of the paper). The services of the bank in restoring confidence and business activity were further compensated by permission to issue a quantity of notes which the government pledged itself to accept as cash without the privilege, which was accorded to individuals, of demanding redemption in coin. The government showed its good faith by devoting to the retirement of the paper money a part of the war contribution paid by France, and 131,829,887 florins were soon withdrawn

[1] Noel, I., 345–46.

from circulation, reducing the amount outstanding to 546,886.38 florins ($273,000,000). The bank continued the process of converting the government money into bank-notes until on December 31, 1847, the amount outstanding was reduced to 9,712,838 florins ($4,850,000).

The uprising in Hungary in 1848, the Crimean War, and the Italian struggle which resulted in Austrian defeat at Magenta and Solferino, imposed new charges upon the Austrian government and did much to upset the work of the bank during the thirty years of peace from 1816 to 1846. The bank had proceeded so rapidly with the conversion of the government paper money as to endanger its own security and alarming runs were threatened in 1831, and again in 1840, which were only averted by the help of the government and in the latter case by a loan of coin from the private banks of Vienna. The charter of the bank expired in 1842, but the Emperor signed a patent renewing its privileges, with some modifications, until December 31, 1866. The bank had enjoyed until this time the exclusive privilege of discount as well as the monopoly of note issues, but the former privilege was now thrown open to others and the power to make loans upon real estate mortgages was withdrawn. The bank had contributed somewhat to the expansion of commerce by its discounts, but its immense advances to the government prevented its applying so much capital as was needed for the development of new private enterprises. Financial societies and private banks of discount had sprung up in the important centres and their success and legality depended upon sharing with the National Bank the power to make discounts and advances.

The bank at the end of the year 1847 possessed a metallic reserve of 70,240,000 florins ($35,000,000) and maintained a circulation of 213,000,000 florins. The outbreak of the revolution in Hungary brought the bill-holders in crowds to the bank for the redemption of the notes and the coin reserve shrunk in a few days to 35,023,030 florins. The directors were seized with panic and secured from the government the decree of June 20, 1848, authorizing the bank to suspend

specie payments and giving forced legal tender character to its notes. The government hesitated to take this desperate step and accompanied it with decrees intended to prevent the export of gold and silver, even to the amount of more than 100 florins ($50) in the pockets of tourists. The government at the same time resumed the issue of its own paper promises in the form of interest-bearing mandates, redeemable in four, eight, and twelve months. The fifth of these issues, in 1849, was given forced legal tender character and the notes were no longer to be redeemed in coin. Gold and silver began to disappear from circulation, pieces of six and ten kreutzers (one to two cents) were coined only to disappear, and bank bills of one florin and Treasury bills of six and ten kreutzers were issued to take the place of the smallest coins. The credit of the bank began to sink with that of the government and the depreciation of the bills in the middle of 1849 to about half their nominal value alarmed the administration and led to a solemn declaration that no more loans should be demanded from the bank and that the existing debt should be adjusted and consolidated.

The history of the thirteen years from 1848 to 1861 is the history of the disregard of this pledge and of repeated loans negotiated through the bank in spite of continual efforts to refund the debt and reduce its proportions. The aggregate of funded and floating debts due the bank by the government was 178,500,000 florins on January 1, 1849, and 205,300,000 florins on January 1, 1850. Considerable reductions were made during the next four years and the figures were carried down to 121,700,000 florins on January 1, 1854. The provisions for the Crimean War forced the figures up again with a bound to 294,200,000 florins ($147,000,000) on January 1, 1855. The reduction of the debt began again the next year and continued until it was reduced on January 1, 1859, to 145,700,000 florins, but the war with the Italian States and France carried the amount up again to 285,800,000 florins.[1] M. Paul Leroy-Beaulieu, after reviewing the

[1] Leroy-Beaulieu, II., 646.

long series of negotiations between the government and the bank, sums up the lesson of these years as follows:

It is apparent how political events hurled the state farther and farther down the path of forced legal tender at the moment when the resumption of specie payments seemed at hand. It is apparent also of what little use were pledges, whether of realty or securities, to hasten the liberation of the state and to permit the bank to terminate the suspension of specie payments. It is because all such pledges are incapable of negotiation at short notice without great loss. It is apparent also what singularly advantageous conditions the bank obtained from the state for its advances. It enjoyed an interest of two or three per cent. on sums in paper which cost it nothing.[1] This situation was too favorable for the bank for it to show itself rigorous towards the state. Every exhibition of complaisance which it made was the source of abundant revenue. This rate of two or three per cent. was extravagant. In France one per cent. was adopted and in Italy six-tenths of one per cent. The transformation, for such a long period of time, of a great establishment of credit into the official lender of the state had the disastrous consequence that this establishment could with difficulty fulfil its natural mission of lending to commerce. One cannot serve two masters, and a bank which always has its hand in its coffers to make advances to the state is compelled to show itself more stringent towards manufacturers and merchants.

The attempt to resume specie payments seemed upon the eve of success in 1859. A monetary convention was concluded January 24, 1857, with the view to securing a uniform currency throughout Germany, by which the contracting parties, of which Austria was one, were to issue no more legal tender paper after January 1, 1859, which was not redeemable in coin on demand. An Imperial ordinance of April 30, 1858, prepared the way for resumption by providing that after November 1st of the same year one-third of

[1] M. Noel seems to ignore this element of the bank loans and says: "The bank, during the entire period which elapsed from its origin to 1861, had risen to the level of its heavy task. It had contributed energetically to sustain the government in the difficult situations which it had traversed and its support, often disinterested, had merited general confidence. Far from abusing the opportunity of the multiplied crises which had obliged the Imperial Treasury to appeal to it, it had endeavored to lighten the burden of the sacrifices imposed by events upon the country."—*Banques d'Émission en Europe*, I., 364.

the new bills should be covered by coin or bullion and that the other two-thirds should be represented in the assets of the bank by securities or commercial paper. An arrangement was also concluded between the government and the bank for the retirement of 100,000,000 florins in small notes by the pledge of the domains of the State. War with Italy upset these carefully laid plans and on April 29, 1859, the bank was again released from the obligation of coin redemption, and the government appealed to it for a loan of 200,000,000 florins. This was met, to two-thirds of its face value, by the issue of bank-notes entirely in denominations of five florins ($2.50). The public had no use for so many small bills and they rapidly returned to the bank. The loan with which it was sought to pay this advance by the bank proved a failure and the government was compelled to deliver a variety of securities in addition to the unplaced obligations of the loan, with a condition that they should not be marketed before November 1, 1861.[1]

The management of the bank decided on May 9, 1853, to issue the 49,379 shares which had remained undisposed of since 1820 and they gave the preference to the holders of the original shares, at the rate of 800 florins payable in bank bills, which were then below par. The bank was again authorized by a decree of October 21, 1855, to loan money on mortgages and issue mortgage bonds. This branch of business rapidly developed and on December 31, 1858, already employed about 37,000,000 florins ($18,500,000). The capital of the bank was again doubled and immediately afterwards increased by 50,000 new shares issued at the rate of about 725 florins, which made the total capital on December 31, 1855, about 110,250,000 florins ($55,000,000). A law of November 13, 1868, reduced the capital again to 90,000,000 florins ($45,000,000).

The approach of the termination of the privileges of the bank led to an earnest discussion, which resulted in the law of December 27, 1862, remodelling the charter of the insti-

[1] Leroy-Beaulieu, II., 650.

tion and its relations with the government. The government proposed the renewal of the charter until 1890; the finance committee of the elective chamber proposed 1880. The subject was referred to a mixed committee of both chambers, which finally fixed the limit at December 31, 1876. The privileges of the bank were broadened from time to time until 1877, when the law of December 20th, terminating the commercial treaties, provided also that the ministry should conclude an arrangement with the bank extending its privileges until March 29, 1878. A subsequent act made the limit May 31, 1878, and one month later the National Bank of Austria was fused with the Austro-Hungarian Bank.

The National Bank, during its later years, in spite of the manner in which it was fettered by its relations to the government and the suspension of specie payments, conducted its relations with the business community in such a way as to contribute in a considerable measure to the expansion of industry. The business paper carried increased from about 32,000,000 florins ($16,000,000) in 1848 to 75,000,000 florins in 1854 and 90,000,000 florins ($45,000,000) in 1855. The advances on public securities increased from about 15,000,000 florins in 1848 to 50,000,000 florins in 1854 and 82,000,000 florins in 1855. The discounts increased nearly forty per cent. from 1865 to 1877 and would probably have reached a larger figure but for the liquidations following the crisis of 1873. The following table shows, in florins, the aggregate amount of the commercial paper discounted every alternate year from 1865 to 1877:

YEAR.	AT VIENNA.	AT AUSTRIAN BRANCHES.	AT HUNGARIAN BRANCHES.	TOTAL.
1865	383,648,611	63,924,852	23,563,202	471,136,665
1867	183,330,404	76,028,931	37,340,086	296,699,422
1869	232,424,629	125,830,418	103,590,858	461,845,906
1871	331,436,438	173,573,951	134,386,521	639,396,911
1873	468,286,132	240,007,674	168,973,050	877,266,856
1875	310,430,552	221,522,518	147,671,119	679,624,190
1877	298,706,477	212,324,840	135,296,195	646 327,512

The provisions for regulating the note issues which were adopted in 1863 bear the traces of the English legislation of 1844. They provided for an "uncovered" circulation of 200,000,000 florins ($100,000,000) and that all notes issued beyond that sum should be covered by gold or silver coin or bullion. The uncovered circulation was required to be protected by commercial paper, by securities deposited for advances, by the coupons of mortgages matured and payable or by mortgage bonds of the bank. This last form of securities was not allowed to exceed 20,000,000 florins and they were accepted for only two-thirds of their nominal value. Gold coin or bullion was at that time allowed to take the place of silver to the extent of only a quarter of the metallic reserve. A decree of October 30, 1868, authorized the bank to count as security for the uncovered circulation bills of exchange drawn upon foreign places, and a law of March 18, 1872, gave the bank discretion as to the proportion of gold and silver to be kept in its reserves.

The attempt to tie the note circulation rigidly to deposits of specie broke down as completely in Austria as it has broken down in England every time that a crisis has occurred. The first suspension of the limit was authorized by the government for a brief period in 1866. The bank was compelled again in 1869 to suspend advances upon private deposits of bullion and did not resume this branch of its business for two years, in spite of the protests of manufacturers and brokers. The bank pursued a very conservative course while the fever of speculation was upon the country, but was unable to come to the rescue of mercantile credit when the crisis of 1873 broke out, because of the limitations upon its circulation. The condition of credit became so critical that the government was obliged to intervene in almost precisely the same manner as in England. A letter was addressed to the bank by the Minister of Finance on May 13, 1873, revoking the provisions of Article 14 of the statutes of the bank, relative to the metallic security for bank-notes, and an ordinance to the same effect was approved by the Diet. The ordinance gave the bank authority to issue notes

by discounting bills of exchange and making advances on public securities without any other limitation than its own good judgment. Under this authority the bank granted extraordinary credits to the amount of 64,451,000 florins in Austria, and 30,119,000 florins in Hungary. The circulation exceeded the legal limit several times in May and July and was almost continuously above the limit during October, November, and December, 1873. The effect of the action of the bank was almost instantaneous in restoring credit. "The first moment of panic passed," says M. Clément Juglar, "it was seen that commerce and industry continued to make good head and that the vital forces of the country were not exhausted, the crisis having been specially severe in everything affecting the bank." [1]

Payment in coin on demand was nominally the condition upon which the bank held its privileges, but the situation of the government and its relations with the bank were such that it was thought necessary to maintain forced legal tender for an indefinite period. A convention was signed between the bank and the government on January 3, 1863, providing for the resumption of specie payments by the bank during 1867, but the war with Prussia postponed the event and the country continued to stagger through the mire of irredeemable paper. An act of May 5, 1866, authorized the government to issue 150,000,000 florins in government bills, including notes of one and five florins which had already been issued by the bank and which were now declared to be bills of state. The disasters of Sadowa and the other events of the war drove the government to the old device of John Law and the French revolutionists, to guarantee a part of its paper issues by the salt mines of Gmund, Hallein, and Aussee, at the same time that the pledge was given that the maximum of the two forms of the floating debt—the paper money and the salt notes (*Salinenscheine*)—should not exceed 400,000,000 florins. This pledge was not kept to the letter, but the actual circulation was never greatly above the

[1] *Des Crises Commerciales*, 496.

legal maximum. The mean circulation of the old paper money in 1876 was 343,029,232 florins and of the salt notes 68,970,395 florins.

An effort was made in 1867 to bring Austria within the circle of the Latin Union and to harmonize her monetary system with that of France, Italy, Belgium, and Switzerland. The government consented to the coinage of pieces of eight and four florins in gold, equivalent to pieces of twenty and ten francs ($4 and $2). The Franco-German war arrested the negotiations before they had been ratified, but the Imperial government immediately began the coinage of the proposed pieces, and they were accepted in France in public depositories by virtue of a decree of June 14, 1874. Their coinage averaged about 3,000,000 florins ($1,500,000) per year, until it was suspended by the laws which reorganized the monetary system in 1892.

The domestic troubles which broke out in Austria before the defeat of Sadowa led to the reorganization of the Empire according to the system of dualism which now prevails. The Hungarian Diet was convoked at Pesth on November 19, 1866, and a basis of union with Austria upon the conditions of local independence was prepared by a committee of sixty-seven headed by Francis Deak. The Hungarian budget was to be entirely independent of that of Austria in all internal affairs except those affecting the army. The officials of the bank regarded their interest as fully protected in both Austria and Hungary by the law of 1862, but the bank soon found its rights in Hungary called in question and sought a new arrangement which would place them beyond attack. The Hungarian Diet passed a vote early in 1870, promising recognition to the bank until the expiration of its privileges in 1876, if the bank would consent to a payment to Hungary in the same proportion as that made to Austria, and if it would establish at Buda-Pesth an independent directorate for Hungary. The bank was willing to make a payment of 4,500,000 florins, but this was not acceptable to the Hungarian cabinet and the privileges of the bank approached expiration without an agreement. The Imperial government

then brought forward a plan for terminating the existence of the National Bank of Austria and substituting in its place a new institution to be known as the Austro-Hungarian Bank. The proposition became law and the new institution was established for a term beginning July 1, 1878, and ending December 31, 1887. The charter was afterwards renewed for a period of ten years ending on December 31, 1897.

The new bank succeeded to all the transactions of the old and a directorate was established at Buda-Pesth and a sum of 50,000,000 florins ($25,000,000) set aside for discounts and advances in Hungary. The bank-notes of the institution are required to be printed in both the German and Hungarian tongues and to bear the arms of the monarchy. The governor of the bank is named by the Emperor, upon the joint nomination of the finance ministers of Austria and Hungary, and the two deputy governors are chosen from the two parts of the Empire. The changes made in the provisions for the note circulation had in view the new character of the bank as a representative of the two monarchies and the purpose of the government to resume specie payments. The certificates and matured coupons of the Austrian and Hungarian debt were included among the legal securities for the covered circulation and it was provided that the two principal establishments at Vienna and Buda-Pesth might issue bills on deposits of silver coin and bullion at the rate of forty-five florins to the pound of fine silver. This provision became inoperative when the government in 1879 suspended the coinage of silver on private account.

The amount of 200,000,000 florins has been steadily adhered to as the limit of the uncovered circulation, but the rule is now followed of keeping coin and foreign gold bills to the amount of forty per cent. of the entire volume of bank-notes in the hands of the public. The difficulties caused by a rigid limit of circulation in 1873 were guarded against, upon the extension of the bank charter in 1887, by the adoption of the German system of the five per cent. tax on the circulation. The method of determination is substantially the same as in the case of the German Imperial

Bank. Weekly reports are required, and upon the amount by which the aggregate circulation exceeds the sum of the metallic reserve and the uncovered circulation of 200,000,000 florins, a tax is levied of $\frac{5}{4}$ of one per cent. for the weekly excess. The notes of the Austro-Hungarian Bank are a legal tender throughout the Empire for their full nominal value in all payments to be made in Austrian money, in the absence of a specific contract or a judicial decision requiring payment in specie.[1]

The authorized limit of circulation has been exceeded on several occasions since the law levying the five per cent. tax on the excess and the tax has been levied for fifteen different weeks. The first occasion was in the autumn of 1890, when the limit was exceeded 656,440 florins in the week of October 7th, and the excess of circulation rose to 23,257,080 florins during the week of October 31st. The excess of circulation declined to 17,093,710 florins in the following week and disappeared in the week of November 14th. The autumn of the next year again required an excess of circulation, which began in the week of September 30th and reached 7,186,560 florins in the next week. This excess was reduced to 223,780 florins in the week of October 15th, and then disappeared, only to reappear in the last week in October and to rise to 13,267,040 florins in the week of November 7th. The amount was reduced in the next week to 3,463,370 florins and disappeared in the week of November 22d. There was a small excess during the closing week of 1891, but none appeared again until October, 1893, when the maximum was 6,767,120 florins for the week of October 31st. This was reduced to 218,120 florins for the week of November 7th and disappeared in the week following. There was no excess of circulation subject to the five per cent. tax during 1894 and 1895.

The essential steps towards the resumption of specie payments in Austria-Hungary were taken by the monetary laws of 1892. The ministers of finance of the two parts of the

[1] Noel, I., 458.

Empire on February 26, 1892, invited a number of eminent financiers and political economists to meet and consider the following questions:

1. What standard ought to be adopted when the currency is reformed?

2. In case of the adoption of the gold standard, should a limited circulation of silver money be admitted and to what amount?

3. Is the circulation of government notes advisable, bearing no interest, redeemable in legal money and not made a forced legal tender, and under what conditions?

4. According to what principles should the conversion into gold of the existing florin be regulated?

5. What monetary unit is it advisable to choose?

The inquiry in Austria was entrusted to a commission of thirty-six persons, under the presidency of Herr Steinbach, the Minister of Finance, and the sittings continued from March 8th to March 17th. The inquiry in Hungary was made by a commission of twenty-one under the presidency of Herr Wekerle. The first question was answered by a large majority in favor of the gold standard. The second question led to a greater division of opinion, but the majority seemed disposed to favor as large a use of silver as was compatible with the absolute maintenance of the gold standard. The majority also favored the continuance of a circulation of 50,000,000 to 100,000,000 florins in government notes not fully covered by coin. A few believers in a strictly metallic currency opposed any such use of paper money, and argued that its continuance would shake confidence in the monetary system. The fifth question was answered in favor of the maintenance of the florin or its division into two parts, if a smaller unit were desired. The answer to the fourth involved the old controversy regarding the effects of the restoration of a metallic standard after business had been conducted and contracts made for many years on a depreciated paper basis. The definite answer to this and the other questions was finally given by the government, without following in all respects the recommendations of the commission.

The proposals of the ministry were submitted to the Parliament of both countries on May 14, 1892, and were made law throughout the Empire on August 11th. The crown (*kronen*) was made the monetary unit upon the basis of cutting a kilogram of fine gold into 3280 crowns, and a kilogram nine-tenths fine into 2952 crowns. The value of the new coin in United States money is 20.3 cents or about one-twentieth more than the French franc. The crown was divided into 100 heller, and gold pieces of ten and twenty crowns were ordered to be coined. Austrian ducats were still authorized to be coined as money of commerce, but the coinage of pieces of four and eight florins under the terms of the treaty with France was discontinued. Silver pieces were provided for of one crown ($0.203) and of fifty heller ($0.1015) and nickel and bronze pieces of smaller denominations. The silver pieces were to contain only 835 parts silver in 1000 parts, making them substantially token coins, and their legal tender quality was limited to fifty crowns ($10).[1]

The government decided to convert the paper money at the rate of one florin for two crowns. This was the rate which was under discussion by the commission, and while it adhered pretty closely to the current rate of exchange it involved a reduction of the nominal value of the paper in gold about sixteen per cent.[2] It had been urged by several members of the commission that it was desirable to convert foreign obligations upon the basis of parity in gold, in order to maintain the public credit, even if it were more just to convert the money of domestic circulation at the rates which had ruled for a dozen years.[3] The problem of conversion was complicated by the fact that the Austrian metallic standard, so far as there had been any, had been silver rather

[1] Ordinance of August 8, 1892, *Bulletin de Statistique*, Sept., 1892, XXXII., 318–22.

[2] Two crowns being worth 40.6 cents, their even exchange for one florin, nominally worth 48.2 cents, left a reduction of 7.6 cents in the value of the florin, which is about 16 per cent.

[3] Raffalovich, *Le Marché Financier en 1892*, 96.

than gold and many obligations were specifically payable in silver. The suspension of silver coinage on private account in 1879 gave a fictitious value to Austrian silver coins, just as it was attempted by the British government to give such a value to Indian rupees in 1893, and the florin ceased to fluctuate with the silver bullion market while remaining below both gold and paper. The government did not in 1879, however, abandon the silver standard and from 1879 to 1891 coined not less than 125,500,000 silver florins at the mints of Vienna and Kremnitz. The rate of conversion adopted for the paper currency, therefore, was not exactly the scaling of a gold obligation, for gold only became the standard on the date that the rate of conversion was fixed. The rate represented about the average exchange from 1879 to 1891.[1]

The bank was required to establish gold payments upon the basis of the new rate of exchange. The result was a considerable benefit to the bank, for it had in its vaults on August 7, 1892, 59,757,000 florins in gold and 20,428,000 florins in foreign bills payable in gold, which at the new rate acquired a higher nominal value. The bank carried 13,500,000 florins in foreign bills to its special reserve fund, and was still able on August 15th to report a cash reserve of 70,666,000 florins, including 619,876 florins received during the preceding week, and foreign bills in hand payable in gold, to the amount of 10,404,000 florins.[2] The addition was made to the special reserve fund in order to avoid increasing the limit of covered note issues, which was not thought advisable without consultation with the government. The entire operation was simply a matter of bookkeeping and added nothing to the real resources of the bank or to the value of its gold. The gold had formerly been counted at its face value, while its real value, expressed in terms of depreciated paper, was much greater. The change simply recognized this fact and in bringing the gold and paper

[1] Haupt, 58–64.
[2] *Le Marché Financier en 1892*, 102.

together gave a nominal value to the former corresponding to the reduced standard. The purchasing power of a given weight of gold remained the same under either method of bookkeeping, but the gold was intended to become under the new system a money of actual circulation instead of a bullion reserve expressed in a standard above the real one.

The importation of gold followed quickly on the establishment of the standard and was promoted by the policy of the bank, which raised the discount rate and made advances to facilitate arbitrage transactions when exchange seemed to be unfavorable. The receipts of gold by the bank from April 11th to October 10, 1892, were 38,759,000 florins ($19,000,000), of which a large part was in pieces of American origin. Receipts from India became heavy in November and raised the total receipts from August 11th, the date of the promulgation of the new laws, to December 31, 1892, to 39,447,000 florins. The state also availed itself of foreign bills in its possession to accumulate gold and at the close of 1892 had about 40,000,000 florins in the hands of the Austrian ministry and 50,000,000 florins in the hands of the Hungarian ministry. A new project was adopted in 1894 for retiring the government paper money and substituting bank-notes and subsidiary silver. An arrangement was made with the Austro-Hungarian Bank to sell 40,000,000 florins in silver for coinage into pieces of one crown and to issue 160,000,000 florins in bank-notes as the government notes were received and cancelled. The Treasury agreed to pay over to the bank 200,000,000 florins in gold ($100,000,000), which was to be used only as the coin guarantee of the new notes, florin for florin. The first notes retired were those of one and five florins and considerable opposition developed among the people at surrendering the convenient paper notes for the more cumbersome silver. An economist of note, Max Wirth, urged that the retirement of paper should begin with notes of 50 florins ($25) instead of the small notes, but the government adhered to its original plan.[1]

[1] Raffalovich, *Marché Financier en 1893–4*, 113.

The crisis of 1893 in the United States and the rather unfavorable condition of the money market in Germany had a reflex influence upon Austria which arrested her steps towards a gold basis and prevented any considerable increase in her gold fund during that year. The reappearance of a premium on gold, running from three to seven per cent., in paper money and bank notes, caused a deal of disappointment and much inquiry as to the reason. The critics of the government ascribed it to the attempt to convert the old five per cent. obligations into four per cents., which resulted in bringing back into Austria a large quantity of securities held abroad. It was calculated that the importations of securities during 1893 exceeded the exports by 114,690,000 florins ($57,000,000).[1] The Minister of Finance pointed out that this inward current was almost wholly in securities payable in silver and that it was necessary to cut the bond which nominally bound the two metals together in the Austrian currency system. A reason was found for the change in some quarters in the state of the money market at Berlin, which was swamped with South American and other securities of little value, which had absorbed the ready money of German capitalists. The Austrian securities were among the few of real value which were held in Germany, and money could be recovered at the smallest loss by returning them to Austria, whose people were buying their own securities at good prices. This tendency, though doubtless heightened in the case of Austria by the conversions and by the fear of payment in silver, only confirmed a principle which has become marked in recent years—that the securities issued by a solvent power tend, after their original placement, to return into the hands of its own people. This was observed in the United States in 1878, when it was estimated that five-sixth of the public debt had returned into the hands of Americans; in France, after the great loans to pay the German war indemnity; and even in Italy, who originally paid two-thirds of her interest

[1] *Neue Freie Presse*, January 1, 1894.

charges abroad, but now pays hardly a fifth outside the Kingdom.[1]

The action of the government in buying silver for subsidiary coinage from the bank is proving a great aid to the latter in solving the problem what to do with its large stocks of silver accumulated when that metal was near the old parity with gold. The cash reserve of the National Bank of Austria and of the Austro-Hungarian Bank consisted almost exclusively of silver while that metal was at a premium over gold, but gold began to flow into the bank in 1871, to constitute about half the reserve. The gold then remained nearly stationary for ten years, while the silver rapidly increased. The efforts to resume specie payments have strengthened the gold resources of the bank, but they are still threatened by the accumulation of silver. The proportion of gold and silver held and other general statistics of the National Bank of Austria and of the Austro-Hungarian Bank appear in the following table:

YEAR.	SPECIE RESERVE. DEC. 31ST. GOLD.	SILVER.	MEAN CIRCULATION.	MEAN CURRENT ACCOUNTS.	MEAN DISCOUNTS.
	(In millions of florins.)				
1865	1.5	120.0	350.0	1.3	—
1870	1.4	112.9	296.8	—	—
1875	67.8	66.5	286.2	1.5	—
1880	65.0	108.3	316.6	1.4	113.4
1883	77.7	121.7	457.7	1.9	144.2
1884	78.8	126.6	358.4	2.1	136.4
1885	69.1	129.7	347.4	2.7	117.5
1887	71.0	145.1	366.0	2.2	129.1
1888	59.0	154.0	384.6	5.6	141.7
1889	54.3	162.2	399.3	7.2	149.2
1890	54.0	165.5	415.6	7.3	156.7
1892	103.2	168.9	425.9	8.3	151.2
1893	101.8	161.9	464.0	11.1	168.3
1894	155.3	139.2	458.9	10.7	151.6
1895	244.0	126.6	619.8[2]	—	246.3[2]

The circulation and the discounts of the bank fluctuate with the seasons. The maximum circulation in 1894 was 517,742,000 florins, for the week ending October 31st, and

[1] Leroy-Beaulieu, II. 228–29.

[2] Actual conditions December 31st.

the minimum circulation was 409,349,000 florins, for the week ending February 23d. The maximum discounts were 190,023,000 florins, for the week of November 7th, and the minimum discounts were 106,841,000, for the week of February 15th. The note circulation on June 7, 1895, was 501,692,640 florins, and the discounts were 150,280,783 florins. The gold reserve on that date had increased to 192,262,330 florins, and the silver had been reduced to 135,093,317 florins. The reserve fund of the bank consists of 32,520,824 florins. The circulation at the close of 1894 consisted of 206,425,360 florins in 10-florin notes, 179,578,800 florins in 100-florin notes, and 121,804,000 florins in 1000-florin notes. The gross product of the operations of the bank in 1894 was 10,440,566 florins, and the cost of administration was 3,801,041 florins, leaving 6,639,524 florins to be divided between the shareholders and the government. A dividend of five per cent. (4,500,000 florins) is first distributed by law among the shareholders, four per cent. of the remainder goes to the reserve fund, the dividend of the shareholders is raised to seven per cent. if the balance permits, and the remainder is divided, half to the shareholders and half to the public Treasury, Austria taking seventy per cent. and Hungary thirty per cent. The government has not realized much from this arrangement, the entire amount in 1894 being only 129,101 florins ($65,000). The amount, moreover, is not paid into the public Treasury, but is set off against a loan of 80,000,000 florins, made to the government in 1863, which was reduced on December 31, 1894, to 76,986,975 florins.

The rate of discount of the National Bank varied between 1817 and 1862 from five to eight per cent., and from 1863 to the fusion with the Austro-Hungarian Bank in 1878 never went higher than six and a half per cent. The changes in the rate of discount during these fifteen years were twelve, while those of the Bank of England were one hundred and fifty-two, of the Bank of France forty-six, and of the Bank of Prussia forty-five. The mean rate of the National Bank of Austria was not more than eight-tenths of a cent above

that of the Bank of England nor more than seven-tenths above that of the Bank of France, in spite of the much more complete industrial development of the latter countries.[1] The rate has varied even less during the seventeen years of the history of the consolidated bank. Fixed at four per cent. on May 9, 1879, it was raised to five per cent. October 20, 1882, reduced to four and a half on February 3, 1883, and to four per cent. on February 23, 1883. The rate was raised again to four and a half on October 7, 1887, and reduced to four per cent. on January 11, 1888. The rate of four per cent. has been pretty uniformly maintained during the early part of the year for the past seven years, but the autumn rate has usually been higher, reaching in 1890 five and a half per cent. An increase from four to five per cent. was made on October 7, 1893, but was followed by a reduction to four and a half in the second half of January, 1894, and to four per cent. on February 9th, where it remained throughout the year and until the autumn of 1895, when it was put at five per cent.

The number of branches of the Austro-Hungarian Bank had risen in 1895 to 34 in Austria and 21 in Hungary, outside the principal establishments at Vienna and Buda-Pesth. The bank at Buda-Pesth has been rapidly gaining in recent years in volume of business over the bank of Vienna, and the development of Hungary from a purely agricultural to an industrial country has created a jealousy which threatens the perpetuation of the bank in its dual form. The discounts at Buda-Pesth, which were 16,853,181 florins at the close of 1875 against discounts at Vienna of 51,109,319 florins, advanced at the close of 1890 to 35,688,570 florins at Buda-Pesth against 53,253,903 florins at Vienna, and at the close of 1894 to 43,410,814 florins at Buda-Pesth against 41,649,846 florins at Vienna.[2]

[1] Noel, I., 382, 434.

[2] *Regelmassige Jahressikung der Generalversammlung der Oesterreichisch-ungarischen Bank, am 4 Februar, 1895*, 31-2. The author is indebted to the courtesy of the officials of the bank for their statutes and full official reports for several years past.

The tendency towards separate local institutions in Hungary has led to considerable discussion of the project of separate banks of issue for the two sections of the Empire and this was one of the reasons why the project for the renewal of the charter proposed by the Imperial Bank in the spring of 1894 was not accepted by the two governments. The bank proposed that the Austrian government reimburse at once the debt of 77,000,000 florins, which is in process of slow reduction by the application of the government share in the dividends. The bank maintained that this reimbursement was required in order to strengthen its position in resuming cash payments. The proposals offered some compensating advantages to the government by giving it a share in the dividends when the net profits exceeded six per cent., instead of seven per cent., as under existing law. The bank asked, on its side, to have the Treasury funds confided to its keeping and to have its capital reduced from 90,000,000 florins to 75,000,000 florins. The bank expressed its willingness to submit at the same time to the supervision of an official board of curators like that of the Bank of Germany, which should control its general policy. The issue of bills, the administration and the policy of the two divisions of the bank were to continue under one head. The issue of bills below fifty crowns ($10) was to be suspended or the subject left open for conference between the bank and the two governments of Austria and Hungary. The charter of the bank was to be continued under these conditions until 1912.[1]

Complaint is already being made in Austria that the withdrawal of the government paper money will produce a contraction of the currency which will prove a detriment to industry and trade. Gold has not yet appeared to any considerable extent in the circulation and the silver pieces of one florin are less popular than the paper money which has heretofore been used for daily transactions. The circulation is about 800,000,000 florins ($400,000,000), which affords an average of less than $10 per capita. The Imperial

[1] Raffalovich, *Le Marché Financier en 1894–95*, 152–154.

Bank is restricted, like the Bank of England, to a fixed circulation of 200,000,000 florins in excess of its coin reserve, and the necessity for a larger use of credit instruments has been so keenly felt that the issue of certificates of deposit in even sums has become a subject of serious discussion. The use of checks is not widely diffused in Austria outside of Vienna, Buda-Pesth, and a few other commercial centres, and the proposition to issue certificates of deposit is a part of the general policy of making the public familiar with the use of credit instruments. The Hungarian Bank of Commerce and Industry has taken the initiative and proposes to issue, in place of the savings deposit bonds heretofore limited to a minimum of 100 florins ($50), small coupons running as low as twenty crowns ($4). One of the propositions discussed was to issue certificates bearing interest, but it was evident that these would be inconvenient as a medium of circulation, because of the necessity of computing the interest, and would tend to deprive the depositor of his interest for the benefit of the last holder of the certificate. The plan proposed by the Bank of Commerce and Industry is to compute the interest on sums remaining on deposit and pay only the face of the certificates, making them substantially similar to checks except that they are issued by the bank for even amounts. The coupons in this respect assimilate closely to bank-notes, and afford a good illustration of the narrow line of separation between checks and notes.

CHAPTER X.

THE BANK OF RUSSIA.

Its Essential Character as an Organ of the Government—The Paper Money System of Russia and the Efforts to Return to a Metallic Basis—The Reorganization of the Bank in 1894 and the Effort to Assist Commerce and Industry—Present State of the Circulation and Discounts—The Tendency towards the Gold Standard—The Finlands Bank.

THE Bank of Russia has been so entirely a mere organ of the State from its foundation to the present time that its history is closely bound up with that of the paper issues of the government. The extension of accommodation to industry and commerce has been an element in the business of the bank, but mainly because enlarged issues of paper have promoted commercial movements. Paper money has taken the place of all other currency as a medium of circulation in Russia and while the bank has a considerable store of gold and the Treasury has a greater store, there are no definite indications as yet of a complete return to a specie basis. The reorganization of the bank by M. Witte in 1894, with its provisions for large advances of notes to small farmers, producers, and manufacturers, is intended to be a step towards bringing the bank into closer harmony with the commercial interests of the country; but the hand of the government is placed more heavily than even upon the management of the bank, and the long terms and liberal conditions fixed for these loans involve some elements of danger.

Paper money was introduced into Russia as early as 1768 and was welcomed at first because of its greater convenience

than the copper money of which it was the representative. The pretext was maintained for a time that the paper was simply the coined certificate for the copper, and the notes, which were known as *assignats*, were at a slight premium. Bureaus were established at St. Petersburg, Moscow, and in the provinces for the redemption of the paper, which may be considered forerunners of the Bank of Russia. A ukase of January 10, 1774, prescribed that the limit of 20,000,000 roubles ($15,400,000) should never be exceeded in the issue of paper money. This pledge was disregarded, as most such limits upon paper issues have been, and after the limit had been raised to 100,000,000 roubles ($77,200,000) on June 26, 1786, in order to obtain resources for war with Turkey, the depreciation began. The price of the silver rouble had risen before the end of the century to 1.47 in paper roubles and the prices of merchandise had followed the upward course of the precious metals. The government endeavored to protect itself, at the same time that it recognized the depreciation of the paper, by a ukase of June 23, 1794, raising the capitation tax paid by the peasants, "in view of the fact that the increased price of all products permits them to earn more by cultivation and other work." [1]

The four most serious efforts to rescue the monetary system of the country from the mire of irredeemable paper were made in 1817, 1839, 1860, and 1881. The first attempt was made by means of loans placed both abroad and at home, of which a part of the proceeds was to be applied to the retirement of the paper circulation. The Emperor Alexander I., after the peace of Tilsit in 1810, recognized all the outstanding notes as a public debt, pledged the public faith to their redemption, and declared that no more paper money should be issued. The circulation, notwithstanding these pledges, climbed upward from 577,000,000 roubles in 1810 to 836,000,000 roubles in 1817. It was then that the loans

[1] Paul Leroy-Beaulieu, *La Science des Finances*, II., 656. The rouble is the exact equivalent of four francs in French money ($0.772) and exchange on Paris at par is quoted in the form of 400 francs for 100 roubles.

were issued which had been promised in a decree of May 27, 1810, and the progress of reform was so rapid that the circulation was reduced in 1822 to 595,776,000 roubles. Count Cancrin was then at the head of Russian finances, and he steadily refused to increase the paper circulation during thirteen years, in spite of wars in Turkey, Persia, and Poland. He hesitated, however, at the policy of substituting an interest-bearing debt for the immense mass of paper obligations bearing no interest and did not succeed in raising the value of the paper rouble much above a quarter of the rouble of silver.[1]

The government made the second effort to reduce the volume of paper money by a decree of July 1, 1839, that the paper roubles should be valued at three and a half to a rouble of silver and that a new form of paper should be substituted in this proportion. The new paper was to be known as bills of credit and was to be redeemable in silver and secured by the public domain. The exchange of the *assignats* for the new bills was ordered to take place on June 1, 1843, and a pledge was given to the business community for the credit of the new paper by depositing in the citadel of St. Petersburg in December, 1844, a metallic reserve of 70,464,245 roubles ($54,000,000), which was to be under the control of twenty-four members of the stock exchange. This fund was increased on July 14, 1845, by 12,180,000 roubles, which established a coin reserve of nearly fifty per cent. of the 170,000,000 roubles in bills of credit then outstanding. A limited redemption was maintained and the bills did not drop far below par until the Crimean War, but new issues of credit paper were made even before the alliance with Austria to crush Hungary and 735,000,000 roubles in the new bills were in circulation at the close of the Crimean War in 1857.

The third attempt to extricate the Empire from the evils of a debased monetary standard was connected with the establishment of the Bank of Russia in substantially the

[1] The greatest depression in the value of the *assignats* was in 1815, when 100 silver roubles exchanged for 413 in paper.—Lévy, 200.

form in which it existed from 1860 to 1894. The statutes of the bank were established by a decree of May 26, 1860, and the reserves of several older banking establishments were turned into its coffers and it assumed their engagements. The original capital was 15,000,000 roubles ($12,000,000) and the declared object of the bank was to consolidate the credit circulation and the floating debt of the Empire. The entire ownership and management were in the government, but the capital and reserve funds were declared to be inviobly set aside for the uses of the bank, and the private depositors were guaranteed against confiscation. A third of the profits were to go to a reserve fund, part of which was to be applied from time to time to the increase of the capital stock.[1] The capital was soon increased by this means to 25,000,000 roubles and the reserve fund to 3,000,000 roubles, where they remained until the reorganization of the bank in 1894. The bank had a metallic reserve on May 1, 1861, of 86,000,000 roubles against a circulation of 714,627,069 roubles, but the commercial discounts scarcely exceeded 14,000,000 roubles. The depreciation at this time was about ten per cent. and M. Lamanski, the deputy governor of the bank, proposed a plan for restoring parity and protecting the note issues. He recommended the transformation of the bank into a stock company, with the monopoly of note issue for twenty-eight years, the redemption of notes in coin according to a sliding scale gradually approaching par, and authority to sell the public domains, the forests and the state railways to protect the circulation.[2]

The plan of M. Lamanski was adopted in a measure, the proceeds of a loan of 15,000,000 roubles were carried to the coin reserve of the bank and it was decreed that bills received in payment for the loan should be destroyed and that new bills should be issued only against deposits of coin. A scale of depreciation was fixed which involved the restoration of parity on January 1, 1864. Redemptions proceeded

[1] Clément Juglar, Article "Banque" in *Dictionnaire des Finances*, I., 347.

[2] Winiarski, 57.

for a while without great losses of coin to the bank, and averaged 1,250,000 roubles per month up to January 1, 1863. A run then began for the redemption of the paper, which resulted in a net loss of coin during January of 2,287,000 roubles; February, 4,921,000 roubles; March, 7,723,000 roubles; April, 10,213,000 roubles; May, 10,367,000 roubles; June, 2,233,000 roubles; and in July, 6,751,000 roubles. Various devices were tried to stop the drain, but they were unsuccessful and coin redemption was suspended by a ukase of November 19, 1863. Exchange on Paris, which had risen on October 29th to 396 francs, within four francs of par, fell gradually to 350 francs, about which point it fluctuated for some time. The net result of the effort to restore specie payments was a reduction of the outstanding paper to 634,773,929 roubles on November 30, 1863, and a useless expense to the Treasury of nearly 100,000,000 roubles ($75,000,000).

The bank was entrusted in 1862 with the mission of buying lands for the peasants and was aided by the deposit of the Treasury funds free of interest. These funds were partly employed in commercial discounts, which were so freely granted that the legitimate necessities of commerce were much exceeded and a mass of doubtful paper was left in the hands of the bank in the crisis of 1873. The expansion of credits, however, was chiefly confined to St. Petersburg and Moscow, and the provinces suffered the usual evils of a country endowed with a single great bank,—the lack of capital, of currency, and of facilities for credit. The excess of capital at the centres caused reckless speculation and blind investments in foreign securities, while the excessive issues of paper money gradually found an outlet only after the emancipation of the serfs created a greater demand for currency for wages. One of the difficulties of the situation was the constantly recurring deficit in the public finances, which called for new issues of paper money to fill the void. This difficulty was overcome for a moment in 1870, when the deficit declined to 1,205,116 roubles, and during the next five years, which showed a considerable surplus. The

quotation of the rouble on the exchange market was 330 francs in 1876, or seventeen and a half per cent. below par, when the menace of war with Turkey and of new issues of paper money carried it down in 1877 as low as 234 francs, or a loss of more than 41 per cent.[1]

The new paper issues which were feared soon became a reality, in order to maintain the armies in the field. The circulation had risen on December 31, 1874, to 797,313,500 roubles and the metallic reserve had increased to 231,227,000 roubles. The circulation was reduced during the next two years until it stood on July 1, 1876, at 693,000,000 roubles. The issue of bills of credit on account of the war was 491,000,000 roubles and the net circulation on December 18, 1878, was 1,103,280,185 roubles. A supplementary issue of 96,000,000 roubles in 1879, with the famine and arrest of exports, caused a crisis in 1880 which reduced the revenues of the government and the railway receipts, in spite of high paper prices, and caused the rapid fall of the coin value of the rouble. The change of ministry which resulted from the crisis brought into power M. Abasa, who at once announced a plan for reimbursing the debt of the government to the bank. A ukase of January 1, 1881, ordered that the Treasury pay to the bank without delay a sum sufficient to reduce to 400,000,000 roubles the debt to the bank on account of disbursements for the government; that the remainder of the debt (400,000,000 roubles) be funded by annual payments of 50,000,000 roubles by the Treasury to the bank; that bills of credit be destroyed to the extent of their accumulation in the hands of the bank and with due regard to the needs of the circulation. The first part of this programme had hardly been carried out when M. Abasa was replaced as Minister of Finance by M. Bunge. The rigid policy of reform which had been inaugurated was somewhat relaxed and the bills paid into the bank were kept on hand and subsequently re-issued, instead of destroyed.[2] The circulation

[1] Winiarski, 59–60.

[2] M. Witte, the present Minister of Finance, has been subjected to criticism for employing 92,700,000 roubles ($71,000,000), paid into

was reduced during the ten years from 1878 to 1888 from 1,188,000,000 roubles to 1,046,000,000 roubles, but the value of the paper rouble did not advance materially towards that of gold.

The statutes of the Bank of Russia were submitted to a complete revision in 1894 and an effort was made to make the bank of greater assistance than before in the promotion of industry and commerce. The first article of the new statutes, promulgated on June 24, 1894, declared the purpose of the bank to be "to facilitate, by means of credit for short terms, the movement of commerce and to promote the success of national industy and agricultural production."[1] The new statutes define with considerable precision the accommodation extended to agriculture and industry by the bank. The institution is authorized to open credits and make loans against bills secured by pledges of hypothecation and by agricultural or industrial material, by guarantee, and by other sureties which the Minister of Finance may recognize as sufficient. Loans secured on material are to be made only to acquire supplementary material or renew old supplies, but they are to constitute a lien upon the old material as well as the new. The material obtained by loans from the bank is required, in accordance with the protective policy of the Empire, to be of Russian fabrication, but exceptions may be authorized in certain cases by the Minister of Finance and, in the case of agricultural material, with the concurrence of the Minister of Agriculture. The maximum loan for an industrial enterprise is 500,000 roubles and for a retail mer-

the bank for cancellation, in the construction of the Trans-Siberian Railway.—De Cyon, 183-85. M. Raffalovich, however, credits the government with having known how "not to abuse the issue of paper money," and declares that "when the needs of commerce have required a greater quantity of monetary signs an issue has been made temporarily under the condition of a special guarantee."—*Le Marché Financier en 1893–94*, 140.

[1] *Bulletin de Statistique*, August, 1894, XXXVI., 183. The date here given, and most others in this chapter, are according to the Julian calendar, whose use still prevails in Russia, and are twelve days behind the Gregorian dates.

chant 600 roubles. The maximum term for loans for material is three years, but periodical payments are required when the term exceeds six months. The bank is authorized to accept as security for loans to small farmers, peasants, and mechanics, upon the pledge of their products, the guarantee of the provincial assemblies, institutions of credit (including mutual societies which agree to operate under the rules framed by the bank), and individuals chosen from among the inhabitants of the respective communities who inspire confidence at the bank.

This new policy of the bank has been subjected to severe criticism upon the ground that the Russian people are unused to operations of credit and cannot be trusted to meet in good faith the required payments. The Minister of Finance himself, in his report recommending the new system, referred to the collapses of most of the banks of commerce and of mutual credit which have taken place in Russia during the past twenty years and to the failure of two branches of the Bank of Russia at Kief and Kharkof, which were authorized to advance money to small farmers on the guarantee of two large proprietors and the certificate of the local tribunal that the property actually existed upon which the advance was made. More than 2,000,000 roubles were advanced annually in loans of this sort, but great abuses occurred and it was found that loans were obtained upon products which had no existence by means of false certificates given by the authorities.[1] The government has felt, however, that some losses could be borne in teaching the people the benefits of commerce and of credit and did not hesitate, during the famine of 1892 and the customs war with Germany in 1893, to advance to the suffering peasants some 90,000,000 roubles which were recovered only partially and by degrees.

The danger of loans upon products is increased, in the opinion of the critics of the bank, by the permission that the products on which loans are made may be retained in the

[1] De Cyon, 135–36.

hands of the producers and by the long terms for which the money is advanced. Long-term loans, in the absence of large deposits, can only be made by fresh issues of paper money and M. Witte made declarations in his report as to the effect of such issues strangely like the declarations of Mirabeau when the French *assignats* were authorized and of Secretary Chase when he was urging upon the American Congress the substitution of legal tender government paper for bank-notes.[1] "The value of these bills," says M. Witte, "issued exclusively for a useful object, will be maintained by the productiveness of labor, and the issue of such bills will not influence the quotations of the credit rouble, because in making these issues in a manner responding to the object in view the quantity of securities in circulation will be at the same time increased."

The government of Russia, however, has undertaken a comprehensive policy for the development of the resources and productive power of the country. It has been felt by those who shape this policy that the government should take the initiative in measures which in other countries would be left to private enterprise. This course has been adopted by Russian statesmen, not in ignorance of the laws of finance and political economy, but under the conviction that those laws would not come rapidly into operation to stimulate commercial and credit operations in an agricultural country without the example of the leadership of the state. This conviction is the keynote of the present policy of the Bank of Russia. The government is willing to take steps in making loans to producers which would not be taken by a private financial establishment, because it is willing to risk something of the national wealth for the sake of increasing it, and because the strong hand of the government can be appealed to for the purpose of punishing defaulting debtors. The issue of paper money, through the instrumentality of a great bank, is felt to be a necessary means for supplying the people with that ample supply of monetary signs which proved so

[1] *Vide* Ch. xv.

beneficial to France after the great influx of gold from California and Australia and which has proved so beneficial to Scotland under her system of free banking. The government has not put in jeopardy the solvency of the bank by its agricultural loans, for the entire amount on December 16, 1895, was 27,466,804 credit roubles, or about one-eighth of the commercial discounts.

The capital of the Bank of Russia was fixed by the new statutes at 50,000,000 roubles ($38,000,000), and the limit of the special reserve was increased from 3,000,000 roubles to 5,000,000 roubles. It was proposed at first to raise the new capital by setting aside annually ten per cent. of the profits, but this process was soon regarded as too slow and a decree of February 6, 1895, provided for taking the necessary amount from the surplus in the Imperial Treasury.[1] Losses by the bank are met from the reserves, and, in case of their exhaustion, are to be carried to the debit account of the Treasury. The management of the bank is entrusted to the Minister of Finance and the annual accounts are submitted to the Imperial Council.[2] The number of branches at the close of 1895 was 107.

The accounts of the Bank of Russia are stated in a similar manner to those of the Bank of England, in the separation of the issue from the banking department. The bills of credit are government notes for all practical purposes and the bank itself, even in its banking operations, is little more than a bureau of the Treasury. A circulation of 769,342,911 roubles is based upon government obligations and corresponds to the "authorized circulation" of the Bank of

[1] *Bulletin Russe de Statistique*, April, 1895, 220.

[2] M. Witte, the present Finance Minister, has also created a board of Treasury officers known as the Council of the Bank and corresponding, according to his view, "to the similar councils in the central banks of Western Europe." These boards take the place of the Council of Imperial Institutions of Credit, created in 1817, which contained representatives of the nobility and of the business community, and the change is criticized by M. de Cyon on the ground that it has brought the bank entirely under official supervision with no external check.—*M. Witte et les Finances Russes*, 145.

England. Circulation beyond this amount is represented by the coin reserve of the bank and can be increased only by deposits of coin. The banking department was utilized for several years for swelling the paper issues in much the same manner as when the suspension of the bank act is authorized in England. These special issues consisted for the most part of the notes which the bank was ordered to call in and destroy by the ukase of 1881, but which were kept in reserve until special authority was given for their re-issue against new deposits of securities or transfers of gold to the cash reserves.[1] The government, by a ukase of December 9, 1894, abolished the distinction between the authorized permanent circulation and the temporary circulation charged against the banking department by transferring the temporary issues from the banking department to the issue department. The limit of authorized circulation without metallic cover was increased by this process from 568,513,000 roubles to 769,342,911 roubles, exclusive of about 285,000,000 roubles covered by gold. Both sides of the account of the banking department were diminished by the amount thus transferred, —200,829,455 roubles,—and by an additional sum of 65,433,-691 roubles transferred in gold from the banking to the issue department as the gold value of that part of the increased permanent issue not represented by securities.[2]

The total gold funds of the bank and the Treasury on January 1, 1895, were 645,731,000 roubles ($500,000,000). This sum was not all in actual gold held in Russia, the sum of 58,331,000 roubles representing foreign credits payable in gold on demand; but the Treasury alone had a gold fund of 194,410,000 roubles and the bank held 39,540,000 roubles in gold in its banking department, exclusive of that held against outstanding notes.[3] The funds then set aside to

[1] Lévy, 201–203.

[2] *Bulletin Russe de Statistique*, Jan.–Feb., 1895, 34–37.

[3] It is interesting to note that 28,654,937 roubles ($21,500,000) of these holdings was in American half-eagles, the largest amount of foreign coin held of a single kind except 38,117,580 roubles ($29,000,000) in English sovereigns.—*Bulletin Russe de Statistique*, March, 1895, 170.

cover the circulation were 351,939,000 roubles and the authorized circulation, covered and uncovered, was 1,121,282,000 roubles ($880,000,000). The government by a ukase of March 3, 1895, increased the metallic coverture for the circulation by transferring from the Treasury to the bank 98,061,276 roubles in exchange funds and substituting 1,125,682 in gold for an equal amount of silver in the bank reserves. This made the total gold funds held against circulation 375,000,000 roubles, exclusive of 75,000,000 held against a special issue, and made the metallic coverture more than a third of the outstanding bills. This is the largest reserve ever held, the amount between 1861 and 1869 having risen from 67,713,000 to 92,884,000 roubles, but in no case higher than 13.6 per cent. of the circulation, and having risen after 1888 to 211,500,000 roubles, or about 20 per cent.[1] The accounts of the bank in recent years are shown in the following table:

YEAR.	MEAN CIRCULATION.	MEAN CURRENT ACCOUNTS.	MEAN TOTAL DEPOSITS.	MEAN LOANS AND DISCOUNTS.
	(In millions of roubles.)			
1880	1,082.3	101.4	295.3	228.5
1885	893.8	132.3	385.9	205.2
1890	902.6	65.6	368.2	213.2
1891	975.3	83.2	399.9	189.4
1892	1,070.0	139.1	438.2	162.8
1893	1,061.9	114.6	405.0	198.0
1894	1,041.5	118.8	495.6	291.7
1895[2]	1,056.9	120.7	545.2	327.5

No official declaration has been made of a purpose to establish the gold basis and specie payments in Russia, but many recent events indicate that the government has its face set in that direction. The credit rouble was originally redeemable in silver, but the free coinage of silver was suspended July 16, 1893, and the credit rouble has remained far above the value of the silver rouble since the great fall in

[1] *Bulletin Russe de Statistique*, March, 1895, 137.

[2] Actual condition Nov. 28th (Dec. 10th by Gregorian calendar). The "Total Deposits" include the current accounts and all other deposits, public and private.

that metal. Customs duties are collected in gold and this gold has been so carefully husbanded that the bank and the Imperial Treasury now possess the largest visible stock in the world. The strengthening of the metallic security for the circulation at the close of 1894 was followed by a ukase of May 8, 1895, of great significance. This ukase declared that written contracts might be made payable in Russian gold roubles and that such contracts might be settled in gold or in roubles of equivalent gold value at the rate of exchange prevailing at the date of payment. Public depositaries were authorized to receive gold at its exchange value in the payment of excises under regulations framed by the Minister of Finance.

The purpose of this law, according to the *Messager Officiel*, is to ameliorate the vices of the *régime* of paper money and "to substitute little by little that of metallic money." With this object, the journal declares, the last two reigns have provided for the collection of customs duties in gold, the reduction (projected in 1881) of the amount of bills of credit, and have taken other steps "which ought to prepare the ground for the re-establishment of a metallic circulation." The new law, it is declared, does not touch the question of the monetary standard or the final basis of adjustment of the paper money to the standard, but is simply intended to give an abiding place in the circulation for gold, which in spite of the large Russian production, has quickly taken passage for foreign countries. The existing circulation of government paper money the official journal found inelastic, unresponsive to the demands for currency at the sale of the crops, and difficult to bring back to the bank when over-issued. The new measure is designed to permit imports of gold when the money market is stringent, by giving gold a legal status in Russian finance, and to liberate the government from the necessity of proceeding to new issues of paper.[1]

The article which announced this policy added the hint of

[1] These statements are abbreviated from the article reprinted in the *Bulletin Russe de Statistique*, May, 1895, 252–56.

another step, which was soon taken, and declared that the new policy would attract foreign capital and inspire confidence in the Russian financial system. The new step was taken by a ukase of June 6, 1895, which authorized the bank to receive deposits of gold coin and bullion and foreign bank-notes and commercial bills payable in gold and to issue certificates therefor, redeemable in gold on demand. These certificates are receivable as the equivalent of gold at the Treasury and the bank, but are not a legal substitute for gold between individuals except with the consent of the creditor. They are receivable at branches of the bank for gold obligations due at other branches and the exchange is furnished free except for the cost of telegraphic service.[1] These important acts were followed on July 26, 1895, by the promulgation of rules permitting the creation of special gold accounts at the bank, for the reception of gold and gold certificates, and the issue of check-books representing payments exclusively in gold. The public are thus being gradually prepared, by the flow of a stream of gold through the Treasury and the banks, for the establishment of gold payments and the maintenance of a fixed relation between the credit rouble and the metallic standard.

The Bank of Russia has established recently a fixed rate of exchange for credit roubles and gold in the ratio of one and a half to one. If this ratio of exchange could be regarded as permanent, and should be maintained in spite of a heavy demand for gold, it would amount substantially to the resumption of gold payments upon the basis proposed by the government of Austria-Hungary in the legislation of 1892. The Bank of Russia has felt strong enough to establish this fixed rate of exchange in order to arrest speculation in credit roubles abroad, which has always become acute at the time for the settlement by foreign purchasers for the agricultural exports of Russia. The bank, by establishing this rate of exchange for gold and paper, has voluntarily abandoned the silver standard, by which the credit rouble would be

[1] *Bulletin Russe de Statistique*, July–Aug., 1895, 27.

worth in gold only fifty per cent. of its face value and about twenty-five per cent. less than its present market value. The attempt to bring the credit rouble to par in gold,—a metal in which it was never redeemable by law,—would depress the price which the farmer receives for his product in credit roubles, while wages and rents would remain substantially unchanged. The position of Russia as an agricultural and exporting country is felt to be adverse to this policy. For this reason, while the Bank of Russia is as strong as any European bank in its accumulation of coin reserves, the Russian government will not for many years attempt the complete retirement of the paper currency.

The Grand Duchy of Finland, which is independent of Russia in its internal affairs, has a bank of issue known as the Finlands Bank, or Bank of the State. The capital is 10,000,000 Finnish marks ($2,000,000)[1] and the bank is governed by managers appointed by the Russian Emperor, who is Grand Duke of Finland, upon the nomination of deputies of the States. The circulation is not permitted to exceed 35,000,000 marks except upon deposits of coin. The actual circulation on September 30, 1895, was 55,547,000 marks; gold reserve, 21,860,000 marks; foreign credits, 31,008,000 marks; loans and inland bills, 26,687,000 marks; deposits, 17,369,000 marks.[2]

[1] The present Finnish coinage system is based upon that of the Latin Union, the markka being the equivalent of the franc ($0.193).

[2] Comptroller's Report, 1895, Letter of Minister Breckinridge, 98–99.

CHAPTER XI.

THE BANKS OF NORTHERN EUROPE.

Development of Banks of Issue in Belgium—The Strain Put upon the National Bank by the Franco-Prussian War—Difficulties Caused by the Double Standard—The Bank of Amsterdam and Modern Banking in Holland—Organization of the Banks of Sweden, Norway, and Denmark.

THE history of banking in Belgium is a history of greater freedom from state interference and entanglement with the finances of the government than that of most other European countries. Belgium began her present national life in 1830 with the assumption of but a small debt as a legacy from her relations with Holland and with the field comparatively clear for the adoption of a sound system of currency and banking. The neutrality of Belgium is practically guaranteed by the great powers of Europe and her military expenditure scarcely exceeds one dollar per capita. The National Bank of Belgium has been employed by the government, therefore, simply as its financial agent in its ordinary transactions and has not been diverted from its duties to industry and commerce by the necessity of floating large loans or covering deficits in the public finances. The government under these conditions has been able to keep in its own hands the ultimate power over the bank, without being often tempted to abuse it, and reserved in the first charter the right to grant to other corporations the power to issue notes. The National Bank has a monopoly of note issue in fact, but is restrained in some measure from abuse of its power by the knowledge that a competitor may at any moment be legally authorized to enter the field.

Monopoly of note issue has existed in Belgium only since 1850. The oldest institution issuing bank-notes was the General Society for the Promotion of National Industry (*Société Générale pour favoriser l'industrie Nationale*). This society was founded in 1822 principally as a bank of circulation and discounts, but it became little by little a great institution of finance interested in promoting investments.[1] The society was a depository of public funds and of large private savings, loaned money on mortgages, on public securities, and on merchandise and was interested as promoter and financial agent in nearly all the large enterprises of the country. It had no strong rival until after the separation of Belgium and Holland and it invited rivalry then by its own shortsightedness. The society and its management were largely under Dutch influence and when the new government of Belgium sought the assistance of the bank as a public depositary the managers refused to make any arrangements which would subject them to the public accounting officers. They regarded the services of the bank as indispensable and forced the government to countenance the creation of a new banking institution more friendly in its character.

The Bank of Belgium was founded February 24, 1835, and the management of the public funds was taken away from the old institution and given to the new. The methods of the new bank had the same defects as those of the old, however, in attempting to make long time loans on commercial paper, while issuing circulating notes payable on demand. The result was a crisis in 1838, when confidence was impaired by the fear of war over the provinces of Limbourg and Luxembourg. There was a violent contraction of credit at Brussels, and the Bank of Belgium found itself without cash to meet its obligations. The older institution, which was somewhat stronger, and was not regarded as so largely a creature of the existing government, took advantage of the opportunity to crush its rival and on December 4, 1838,

[1] Courcelle-Seneuil, 339.

presented 1,000,000 francs ($200,000) to the Bank of Belgium for redemption. They followed this up on December 10th, by the presentation of 1,200,000 francs and on December 15th, by the presentation of 300,000 francs more. The bank was forced to suspend and to appeal to the government for assistance. A loan of 4,000,000 francs ($800,000) was voted, of which 2,600,000 francs were applied to the payment of bills and commercial obligations of the bank, and 1,400,000 francs to meeting the demands of depositors in the savings branches which had been established.[1]

The manner in which the existing institutions mixed up the business of banks of issue and deposit with that of operations for long terms created a strong feeling in favor of a bank devoted exclusively to commercial banking. The Bank of Belgium was again embarrassed in 1842 and was compelled to surrender the privilege of keeping the public monies. An arrangement was entered into between the Treasury and the *Société Générale*, but that institution felt the effect of the crisis of 1842 and was compelled to abandon all the branches which it had established except that at Antwerp. The government, therefore, in view of the necessity for an institution of a different character, in granting a renewal of the charter of the *Société Générale* for twenty-five years, in 1843, reserved the right to revise and restrict its powers before the end of the year 1849. The crisis following the political excitement of 1848 compelled both existing banks to suspend specie payments and afforded the government the best of excuses for curtailing their privileges. The banks were aided for the moment by an act of March 20, 1848, giving forced legal tender character to their bills but confining the issues within fixed limits. The year 1849 had hardly begun, however, when the President of the Council of Ministers, M. Frère-Orban, brought forward a plan for the National Bank of Belgium (*Banque Nationale de Belgique*). The charter of the bank was granted by the law of May 5, 1850, fixing the capital at 25,000,000 francs ($5,000,-

[1] Noel, I., 549.

000), divided into shares of 1,000 francs each, and giving the bank its franchise for twenty-five years. The bank was forbidden to borrow or make loans upon mortgages, or upon deposits of industrial stock, and was forbidden to take part directly or indirectly in industrial enterprises. The administration of the bank was intrusted to a governor appointed by the King for five years and six directors chosen by the shareholders, and a government commissioner was charged with the supervision of discounts and the issuing of bills.

The National Bank found itself face to face with strong competitors in the two older banking institutions, but gradually gained in strength and credit up to 1870, when it was subjected to one of the severest tests ever put upon a banking institution. It was not distrust of the bank, but the political events accompanying the Franco-Prussian War which caused the stress. The demand for banking accommodation was greatly increased by the necessity of furnishing supplies for the hostile armies and many business transactions were transferred to Belgium which would ordinarily have been carried on in France or Germany. This was an evidence of confidence in the bank which would not have been without its benefits if the institution had been prepared for so sudden an enlargement of its transactions, but this indication of confidence from without was offset by a degree of distrust at home which led to the presentation of large quantities of bank bills for redemption in coin. The government added to the dangers of the situation by a policy which tended to embarrass the bank and to increase the uneasiness of the public.

The administration feared that a declaration of war between France and Germany would lead to the violation of the neutrality of Belgium, and directed the National Bank to take measures to transfer the metallic reserve, representing the balance due the Treasury, to the port of Antwerp. The bank was informed on July 13th that this transfer must be effected without delay. An attempt was made to carry out the movement secretly, but the news became public that the metallic reserve had been removed from Brussels and

caused great popular alarm. The government, instead of sustaining the bank, issued two more stupid orders,—one to the agents of the Finance Department in the provinces, not to permit their cash to be exchanged for bank bills, and the other to the chiefs of the military forces, to exchange bank bills in their military chests for coin.[1] Notwithstanding this apparently deliberate effort to discredit the bank, the government refused to permit the suspension of specie payments and held the institution strictly to the performance of the obligations of its charter. The orders regarding the public funds and the military chests were so palpably unwise that they were quickly revoked, and an order was given to pay everything in bank bills which could be so paid, and to exchange large bills at the agencies of the banks for small ones, in order to facilitate payments in bills.

The discounts of the bank increased from 177,500,000 francs on July 10, 1870, to 203,923,100 francs on July 20th, and to 223,231,744 francs on July 31st. While assistance was thus rendered to commercial credit, the presentation of notes for redemption rose from a daily average of 600,000 francs ($120,000) during 1869 to a daily average of over 1,000,000 francs ($200,000) during the eighty-two days from July 1st to September 20, 1870. The amount presented on July 20th was 6,282,000 francs ($1,250,000) and on the next day 7,025,000 francs ($1,400,000), and the daily average from July 15th to July 30th was 2,094,000 francs ($415,000). The bank was able to meet these demands by appeals for loans of coin from London, Amsterdam, Hamburg, and Paris, and by realizing the bills drawn on foreign countries which it had in its possession.[2] These bills, which amounted

[1] Noel, I., 486.

[2] The large holding of foreign bills, chiefly drawn on London, in the cash reserves of European banks is, "to a very large extent, solely for the sake of the interest which is to be made on them. Bills on England, owing to the high rate of interest which they often bear, as compared with continental rates, are a favorite investment abroad. In Paris, Berlin, Frankfort, Hamburg, and other conti-

at the outbreak of the crisis to 64,144,561 francs, were reduced on July 31st to 7,227,333 francs. The proceeds were employed in the purchase of bullion, principally in silver, which the mint rapidly coined into crowns. The bank was thus enabled to meet every demand and to reduce the rate of discount as soon as the crisis was over. The rate of July 15th was two and a half per cent., but this was increased to five per cent. between July 15th and August 5th, and to six per cent. from August 5th to August 27th, and even to seven per cent. for bills drawn in foreign countries on Belgium. The 27th of August saw the worst of the crisis over, and the domestic rate fell to five and a half per cent.; on September 20th to four and a half per cent.; and on October 8th to three and a half per cent.

Belgium was led to propose the formation of the Latin Union in 1865 because of the difficulty of maintaining the double standard under the oscillations in the price of gold and silver. The French system of decimal coinage was adopted by the law of June 5, 1832, but silver was made the standard and no provision was made for gold coinage. The creation of a gold circulation in France after the great gold discoveries led to a popular demand for the admission of French gold coins into Belgium. This was decreed by the law of June 4, 1861, and the result was to drive the silver five-franc pieces out of sight and change the standard of actual circulation from silver to gold. The National Bank had a reserve at that time of 48,645,000 francs in silver five-franc pieces, which was paid out to meet current demands, but this fund declined by November 8, 1862, to 14,629,000 francs, and the bank suspended their further issue.[1] The smaller pieces continued to disappear, but the movement was retarded for a time by the suspension of specie pay-

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nental cities, the bills on England held by the bankers and joint stock companies often amount to many millions sterling; and a very large sum remains in their hands for several months,—in fact, from the time when the bills are drawn to the time when they fall due."—Goschen, *Foreign Exchanges*, 138.

[1] Shaw, 191.

ments in the United States. The drain set in again in 1865, the small silver pieces became so scarce that they could not be supplied by the bank in sufficient sums to meet the demands of manufacturers, and the government was compelled to resort to the coinage of nickel pieces. The Belgian delegates urged the adoption of the gold standard at the conference which resulted in the formation of the Latin Union, but consented to the convention finally adopted by the other powers.

The fall in the value of silver after 1867 dragged Belgium into new difficulties, against which the convention of the Latin Union afforded her no protection. The government was authorized by the law of December 18, 1873, to suspend the minting of silver five-franc pieces, which had been going on at the rate of 300,000 francs a day. The coinage of silver had already exceeded domestic needs, and great quantities drifted across the French frontier and found their way into the Bank of France. This circumstance was made the occasion of a demand at the conference of 1885 that the countries of the Union take back their national coins and pay for them in gold. The Belgian delegate, M. Pirmez, at first refused to consider any such proposition, declared that Belgium was being made the victim of the misfortunes of the Union, and absented himself from the sittings of the conference. He declared that the treaty of 1865 made no reference to any such process of liquidation; that the acceptance of Belgian coins by French citizens had not been a part of the treaty, but a result of voluntary action; and that the dissolution of the treaty would simply relieve public depositaries from further acceptance of foreign coins, without imposing any obligations upon their issuers to redeem them.[1] The fear that the collapse of the Latin Union would imperil the gold standard in Belgium finally prevailed, however, over other arguments, and Belgium consented to a basis of liquidation by which each country was to pay in gold for one-half of its five-franc pieces returned

[1] Ansiaux, 14.

to it and was allowed to leave the other half to be returned by the play of foreign exchange.[1]

The position of Belgium and of the National Bank will be peculiarly embarrassing if the dissolution of the Latin Union destroys the legal status of the silver coins of one country in the others. Belgian coins would under such circumstances flow rapidly back into Belgium and would be likely to glut the reserves of the bank and make difficult the maintenance of the gold standard. The metallic reserve of the bank averages about 100,000,000 francs, of which only a fourth is now in silver, but the volume of Belgian five-franc pieces outstanding is estimated at 400,000,000 francs, of which about 200,000,000 are in the Bank of France, besides those in active circulation in France.[2] A glut of silver in Belgium would have the tendency to draw gold from the National Bank, while there would be the strongest disposition in the bank to retain gold and force silver into circulation. It would put a severe test upon the credit of the bank and its 460,000,000 francs of paper circulation to attempt to enforce the policy of the Bank of France, to redeem in silver at discretion, and the pressure for gold for export would be strong because of the redundancy of the monetary circulation which the glut of silver would cause. The heroic policy of buying gold and selling silver for what it will bring in the bullion market is favored by some Belgian statesmen and may prove the only effective means of maintaining the gold standard.

The present charter of the National Bank of Belgium was granted in 1872, when the life of the bank was extended to

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[1] M. Haupt considers France rather than Belgium the victim in this transaction and regrets that her delegates, after securing the consent of the delegates of Italy, Switzerland, and Greece to liquidation in full in gold, yielded to their demand that they have the same privilege as Belgium of liquidating in gold to the extent of only one-half their silver coins accumulating in French hands.—*The Monetary Question in 1892*, 90.

[2] Haupt, 93.

January 1, 1903, and the capital was increased to 50,000,000 francs ($10,000,000). Several changes were made in the previous laws regarding taxation, the handling of the public funds, and the share of the government in the profits of the bank. Greater precision was introduced into the provisions regarding the proportion of specie held, which is now required to be one-third of the notes in circulation and of other demand liabilities. This reserve may be trenched upon in emergencies with the consent of the Minister of Finance. The notes of the bank were made a legal tender by the law of June 20, 1873, but only so long as they are redeemed in coin on demand and are receivable in public depositaries. Their acceptance by public depositaries is defined by law, but may be suspended by the Minister of Finance.[1] A portion of the public funds in the custody of the bank is allowed to be loaned, but the profits earned go to the credit of the Treasury. The government levies a patent tax on the gross volume of business of the bank, a stamp tax on the notes, and a tax of one-fourth of one per cent. on the circulation above 275,000,000 francs; and also receives the product of discounts at rates above five per cent. to the amount of the excess, and one-fourth of the net profits of the bank in excess of six per cent.[2] The leading items of the accounts of the bank since its foundation are shown, in francs, in the following table:

DEC. 31st.	CIRCULATION.	METALLIC RESERVE.	DISCOUNTS.	DEPOSITS.
1851	50,346,210	29,264,880	44,034,953	25,980,830
1860	117,899,960	63,023,535	155,958,745	81,825,144
1870	202,528,520	95,614,523	196,233,878	81,319,921
1880	339,969,510	98,787,206	283,992,826	72,142,896
1890	404,721,600	103,413,340	312,670,661	67,723,926
1892	427,594,580	114,654,737	309,391,705	69,340,318
1894	469,662,000	130,756,515	346,590,227	78,558,169
1895	461,850,000	103,325,000	397,850,000	74,300,000

[1] Noel, I. 526.

[2] Noel, I. 563.

The Bank of The Netherlands.

The existing Bank of the Netherlands is the successor of the Bank of Amsterdam, one of the most famous of the banks of the Middle Ages. The Bank of Amsterdam was not a bank of issue in the modern sense, but proposed originally to deliver receipts for deposits of coin. The bank was founded by an ordinance of the City of Amsterdam of January 31, 1609, and was called the Exchange Bank (*Amsterdamsche Wisselbank*). Much confusion and many disputes had arisen in the city because of the variety of coins in circulation and their departure from the proper standard. Money of full weight rose to a premium with the exchange brokers and the fact was considered as the result rather than the cause of their operations. The city undertook by a statute of July 15, 1608, to prohibit the holding of deposits or the transfer of money by any one except the owners or their personal agents. The use of bills of exchange was forbidden and traders were directed to make no discrimination between light and heavy coins nor to give or take money at a higher rate than that fixed by the States-General.

These provisions were only intended to clear the ground for the establishment of the new bank under government control. All bills of exchange were required to be paid through the bank, and the institution was required to sell any kind of specie demanded of it at as low a premium as possible. The transferable deposits or credits came to be known as "bank money" and bore this designation throughout the history of the bank. The creation of a means of exchange of fixed and uniform value did much to promote the great commerce of which Amsterdam was becoming the centre. The bank accepted deposits only at their bullion value and granted credit for the amount in lawful money, subject to a proper charge for handling. Deposits were necessarily subject to charges, because the bank was supposed to keep in its vaults every guilder received and to do no loan and discount business. Payments in Amsterdam came to be made universally in bank money, by the pre-

sentation of a transfer order at the bank by the payer or his authorized agent, which entitled the payee to the credit on the next day. The bank became so general a medium of payments in Amsterdam that the most extravagant estimates were formed of the gold and silver stored in its vaults. Some put the amount as high as 900,000,000 gulden ($360,000,000) but the more modest and accurate estimate of Adam Smith was 33,000,000 gulden ($13,500,000).[1]

Direct redemption of bank credits in coin gradually fell into disuse, partly because bank money was so much preferable to coin for nearly all practical purposes and partly because of the acceptance of foreign coins on special deposits. The system of advances upon such deposits was formally put in operation in January, 1683, and the bank issued a receipt to the depositor for the bullion value of the deposit, certifying his right to withdraw it upon returning the bank money with which he had been credited and paying one-eighth of one per cent. interest. The right of withdrawal was forfeited if the charges were not paid and the deposit renewed within six months. It was necessary, therefore, in order to withdraw coin thus deposited, to have both the receipt and the equivalent amount of bank money. The bank money outstanding was in excess of the legal coin in the custody of the bank, but not in excess of the domestic and foreign coin and bullion. The lapsing of receipts protected the bank, therefore, from demands for coin redemption which it could not meet, while another method was adopted to prevent the excess of the bank money in circulation and to provide bullion for those who desired it for export.

The method adopted by the bank for controling the volume of circulation and maintaining its credit was the sale of bank money for specie or specie for bank money in such amounts as the public might require. Regular agents of the bank were charged with these transactions and kept the premium on bank money within narrow limits and its value substantially unchanged. It was supposed until the last

[1] *Wealth of Nations*, II. 61.

half of the eighteenth century that the bank had sacredly fulfilled its obligations to keep in the vaults the exact amount of coin and bullion represented by the bank money outstanding. The affairs of the bank were kept secret by the small committee of the city government which was charged with its administration, and it was not generally known that as early as 1657 individuals had been permitted to overdraw their accounts and that in later years enormous loans of specie had been made to the Dutch East India Company. The truth became public property in the winter of 1789 and 1790. The premium on bank money, which was usually kept above four per cent., then fell below two per cent. and in August, 1790, disappeared. The bank failed to protect its credit by purchasing bank money on an adequate scale and it was represented that large purchases would be followed by a heavy export of bullion to the injury of commerce. The possibility of deception came to an end when on November, 12, 1790, a notice was issued that silver would be sold to the holders of bank money at a rate equivalent to ninety per cent. of their claims. It was substantially an admission of insolvency and the debt was assumed in 1791 by the government of the City of Amsterdam. The effort was made to put the bank again on its feet, but the time for such banks had passed, the position of Amsterdam as a commercial centre had changed, the bank was closed by a royal decree of December 19, 1819, and the small amount of bank money outstanding was soon after paid off.[1]

The Bank of the Netherlands (*de Nederlandsche Bank*) was authorized by the government in 1814, after it became evident that the Bank of Amsterdam could not be revived. The privilege of the bank was twice renewed for twenty-five years, carrying its charter to March 31, 1889. The last renewal was nominally only for fifteen years, until March 31,

[1] A summary of the result of the researches of the latest scholarship regarding the Bank of Amsterdam, based in part upon the history of the bank by W. C. Mees, formerly president of the Bank of the Netherlands, is presented by Prof. Dunbar in his valuable work on *The Theory and History of Banking*, 82–105.

1904, but a further renewal for ten years will be tacitly assumed unless the abrogation of the privilege is decreed by the State.[1] The law of December 22, 1863, left open the possibility of establishing other banks of issue by special law, but the Bank of the Netherlands has been in fact the only bank of issue in Holland since its establishment. The capital of the bank was originally 5,000,000 florins ($2,000,000) and has been increased from time to time to 10,000,000, 15,000,000, and 16,000,000 florins ($6,400,000). The bank is not a public institution, but the State subscribed in 1863 for one thousand shares at 115, which were sold on June 1, 1864, at 190. The government exercises a supervision over the affairs of the bank through a special commissioner paid by the bank, and the president and secretary are named by the King. The Treasury does not share directly in the profits of the bank, but collects an impost in the nature of a patent tax proportional to the dividend distributed. Five per cent. dividends are provided for the shareholders, which are to be made up from the reserve fund in case of insufficiency of the profits. The bank performs gratuitously the duties of agent of the Treasury at Amsterdam and includes the Treasury resources in its deposit accounts.[2] It is limited to the usual operations of a bank of issue, discount, and deposit and is forbidden to take part in any commercial or industrial enterprise or to make advances upon real estate.

There is no fixed limit upon the note issues of the Bank of the Netherlands, but the decree of August 16, 1884, fixed the proportion of the metallic reserve at forty per cent. of the aggregate of notes and deposits. The law imposes no restrictions on the proportion of gold and silver, but since 1872 the bank has ceased to buy silver and has added as much as possible to its gold. Holland suspended the free coinage of silver in December, 1877, and has maintained her monetary system at parity with gold by treating the silver coins as tokens, redeemable in gold. The Bank of the

[1] Lévy, 194.

[2] Alfred Neymarck, Article "Banque," in *Dictionnaire d'Économie Politique*, I., 144.

Netherlands held 42,996,000 florins in gold on December 28, 1895, and 82,164,000 florins in silver. The principal office of the bank is at Amsterdam. There is a branch at Rotterdam, and there are thirteen agencies and correspondents of three different classes in fifty-six other localities. The circulation of the bank has gradually increased from a mean of 104,859,994 florins in 1865, to 131,656,347 florins in 1870, 175,340,677 florins in 1875, and 203,600,000 florins ($82,000,000) in 1895. The issue of notes below ten florins ($4) is prohibited.

The monetary system maintained by the Bank of the Netherlands is of peculiar interest, because of the demonstration which it affords that, within narrow limits at least, it is possible to maintain the gold standard with very little gold and while the money of circulation is chiefly of silver and paper. The bank pursues a policy directly opposite from that of the Bank of France, by furnishing gold freely for export and sparingly for domestic circulation. The purpose of this policy is to maintain the parity of foreign exchange, because of the conviction that a refusal to furnish gold for export would put the metal at a premium and precipitate the country upon a silver basis. This danger was a serious one in 1883. The gold reserve, which had been at 56,924,000 florins at the close of 1880, declined in October, 1882, to 11,306,638 florins and in February, 1883, to 5,365,091 florins ($2,150,000). A bill was promptly introduced in the States-General, authorizing the melting of 25,000,000 florins in old pieces of two and a half florins and their sale as bullion, in order to obtain gold. The bill did not become law until March 4, 1884, but the exchanges in the meantime became favorable and the stock of gold rose on April 21, 1883, to 31,000,000 florins ($12,400,000). The bank now stands ready to furnish gold for export or to furnish silver at its bullion value, while the old stock of large silver coins is being gradually reduced by subsidiary coinage for Holland and Java.[1]

[1] *Bimetallism in Europe*, Sen. Ex. Doc. 34, 50th Cong., 1st Sess., 33.

The Banks of Sweden and Norway.

The three countries of the Scandinavian Union,—Sweden, Norway and Denmark,—have a uniform monetary system based upon the gold standard with the crown as the unit, worth twenty-six and eight-tenths cents ($0.268) in United States money, but each country has a banking system of its own. The State Bank of Sweden (*Sveriges-Riksbank*) was founded November 30, 1656, and to Palmstruch, its founder, is attributed the first use of bank bills as credit money, not fully covered by the coin reserve. The bank became a public institution in 1668, and its capital is furnished by the nation, but the administration is under the charge of a commission chosen by the Diet and is not responsible to the executive department of the government. The capital of the bank is 25,000,000 crowns ($6,700,000) with a reserve of 5,000,000 crowns, and it is allowed to issue notes to the amount of both, plus its credits with foreign banks and its metallic reserve.[1] The reserve is not allowed to fall below 10,000,000 crowns. The notes are a legal tender by the Swedish constitution in Sweden and are receivable by public depositaries, and in these respects have an advantage over the notes issued by the private banks of issue.

The private banks number twenty-seven and may be established by royal authority. The original legislation on the subject (January 14, 1824) required the number of shareholders in each bank to be not less than thirty. A new law of January 1, 1887, imposed certain general conditions upon the private banks, which are still in force.[2] The capital of each is required to be at least 1,000,000 crowns ($268,000), the charter runs for ten years, and the shareholders are no longer responsible except for the amount of their shares. The circulation is limited to the aggregate of the capital invested in securities, the reserve similarly invested, half the total of credits of the bank, and the coin reserve, after the deduction of an amount equal to ten per cent. of the

[1] Muhleman, 74.

[2] Lévy, 219.

capital. These banks are required to redeem their notes in gold upon demand and are not authorized to substitute bills of the State Bank. Five of the banks have branches at Stockholm, where they exchange their bills for those of the Bank of Sweden, which can be turned into gold upon demand.

The note circulation of Sweden under this system of comparatively free banking has been kept within prudent limits and the notes circulate at par with coin. The circulation of the Bank of Sweden on August 1, 1895, was about 54,000,000 crowns and of the private banks 64,000,000 crowns (making a total of $30,000,000). The metallic reserve of the Bank of Sweden was 31,000,000 crowns and of the private banks 20,000,000 crowns. The Bank of Sweden carries about 27,000,000 crowns of this amount in gold, but the private banks have only 8,500,000 crowns in gold. The discounts of the Bank of Sweden were 35,500,000 crowns, advances 55,000,000 crowns, and current accounts 38,500,000 crowns. The discounts of the private banks were 180,000,000 crowns, advances 155,000,000 crowns, and current accounts 400,000,000 crowns. The Bank of Sweden, in spite of its public ownership, is not deeply involved with the obligations of the government, but is the depositary of the public funds and makes an annual advance, by vote of the Diet, of about 1,600,000 crowns to facilitate the operations of the Treasury.[1]

The Bank of Norway (*Norges Bank*) was founded June 14, 1816, with its head office at Drontheim and branches in leading towns of the province. Its capital was raised by a tax upon landed property and the land-holders became shareholders in the bank according to their respective payments. The original capital of the bank was 2,000,000 specie dollars and circulation was issued provisionally in the proportion of five dollars to two dollars of the capital. One of the purposes of the foundation of the bank was the improvement of agriculture, and the discount of commercial

[1] Neymarck, Article "Banque," in *Dictionnaire d'Économie Politique*, I., 144.

bills was at first only a secondary consideration. Loans were made by means of note issues upon land to an amount not exceeding two-thirds of the valuation, and the borrower made a semi-annual payment, including not only interest, but five per cent. annually of the principal, which was thus liquidated in twenty years, like some modern mortgage loans. The attempt to float a paper currency upon land values resulted in failure and the notes of the bank in 1822 could be exchanged at Hamburg at the rate of only $187.50 for $100 in silver. The Storthing was compelled to pass a law reducing the value of the notes by providing that 190 in paper should be redeemed in the proportion of 100 in silver.[1] The value of the notes gradually rose and the bank was put upon a sounder basis. The present capital is 10,000,000 crowns and the note issues are limited to twice the reserve, of which one-third may consist of deposits with foreign banks. The notes are legal tender in Norway and constitute the only credit paper of general circulation. The governing board of the bank is named by the Storthing and consists of fifteen representatives. The actual administration is entrusted to five directors at the central bank and three at each branch, who are also named by the Storthing. The State is a large shareholder, but the management of the bank is kept independent of the Treasury.[2] The circulation on August 1, 1895, was about 60,000,000 crowns ($15,000,000), the metallic reserve 30,000,000 crowns, discounts 34,000,000 crowns, advances 20,000,000 crowns, and current accounts 9,000,000 crowns.

The National Danish Bank.

The National Danish Bank was found in 1818 and has a capital of 26,752,400 crowns ($7,000,000).[3] The bank was the successor of the State Bank (*Rigsbanken*), which had been created by the government in 1813 to restore order to

[1] Macleod, *Theory and Practice of Banking*, II., 263-64.

[2] *Statistique Internationale des Banques d'Émission:* Norvège, 6-7.

[3] Lévy, 218.

the demoralized financial system of the country. A decree of July 4, 1818, transferred the privileges of the old bank to the new for a term of ninety years. The government is free at the end of this period, in 1908, to extend the privileges or revoke them. The capital of the National Bank is in private hands, but it was collected by an enforced levy upon real estate, and the land owners became shareholders in the bank for the amount of the tax paid. The bank assumed the obligations of the State Bank and was unable to pay dividends until 1845. The dividends since that time have averaged about seven per cent. The note circulation has no fixed limit, but is subject to conditions as to the amount of reserve held. A decree of 1873 fixed the limit of circulation not fully covered by specie at 27,000,000 crowns, but this was increased by a decree of November 5, 1877, to 30,000,000 crowns. The metallic reserve is not permitted in any case to fall below three-eighths of the face value of the notes, and at least 12,000,000 crowns must be in gold coin or in bullion which has been actually delivered to the mint for coinage. The other portions of the metallic reserve may be in gold bars or foreign gold coin and in foreign silver to an amount not greater than one-third of the entire fund.[1] Redemption of notes is required in gold coin on demand. The notes are legal tender and are the only credit paper in use as currency in the Kingdom. The circulation on July 31, 1895, was about 83,000,000 crowns ($21,000,000); specie reserve, 60,000,000 crowns; discounts, 20,000,000 crowns; current accounts, 19,800,000 crowns; advances, 35,000,000 crowns.

[1] *Comptroller's Report, 1895*, Report of Minister John E. Risley, 77.

CHAPTER XII.

THE BANKS OF SOUTHERN EUROPE.

Development of Banking in Switzerland—The Proposed Bank of the Swiss Confederation—The Bank of Spain and its Entanglements with the Treasury—Similar Situation of the Bank of Portugal—The Greek Banks and the Effects of Specie Suspension—The Ottoman Bank—The Banks of Roumania, Bulgaria, and Servia.

BANKING in Switzerland had its earliest development at Basle and Geneva, which were long noted for the skill and wealth of their bankers, but banks of issue were not established in either city until 1845. The first Swiss bank of issue was established at St. Gall in 1836. The cantonal bank of Vaud and the Bank of Basle were established in 1845, the Bank of Commerce at Geneva in 1846, and the Bank of Geneva in 1848. The incorporation of banks of issue rapidly spread among those cantons which contained a considerable number of merchants, and in 1863 eighteen banks had been established, with forty-two agencies or branches. The aggregate circulation of these banks on December 31, 1862, was 18,468,122 francs ($3,600,000), the cash reserve was 19,380,922 francs and the current accounts, representing deposits, 49,166,405 francs ($9,800,000).[1] Eleven of these eighteen banks were established with the help of the cantonal governments and the remainder were established by private funds.

The Swiss banks preserved until 1875 a purely local existence and their operations and circulation rarely extended beyond the limits of the canton in which they were estab-

[1] Courcelle-Seneuil, 350.

lished, but the growing needs of commerce invited co-operation and the extension of banking facilities. Some of the banks began to extend their branches into other cantons and others made conventions with each other for the mutual acceptance of their bills. It was at this stage in the development of Swiss banking that the Federal constitution was revised and authority to legislate regarding banks confided to the Federal government. Protection against monopoly was afforded by the provision of the constitution that Federal legislation "shall not establish a monopoly of the issue of bank bills nor decree their obligatory acceptance." The law of 1875 required the Swiss banks to maintain a cash reserve equal to forty per cent. of their notes in circulation and forbade any one bank to issue circulation in excess of 12,000,000 francs ($2,400,000). Each bank was required to accept the notes of other banks and to redeem them in coin. The number of banks at the end of 1873 was twenty-eight and their circulation was 47,606,000 francs ($9,400,000), against which there was a cash reserve of 14,892,796 francs.

The Act of 1875 was superseded by that of March 8, 1881, which limited the circulation to double the paid-up and unimpaired capital (*capital versé et réellement existant*) of the banks and required banks of issue to have a capital of at least 500,000 francs. The requirement of a forty per cent. cash reserve was maintained, to be distinct and independent of the other reserves of the bank and kept in a separate account. The remainder of the circulation was required to be fully covered by the deposit of securities or commercial bills. Weekly, monthly, and annual reports are required according to a form prescribed by the Federal Council and an annual examination is made under public authority.[1] The notes are issued through the Federal inspectorate, are delivered to the banks as they need them, and are of a uniform type. A bank which renounces its circulation is required to redeem the notes for a certain time, to surrender the redeemed notes to the Federal authorities and after the

[1] Alfred Neymarck, Article, "Banque," in *Dictionnaire d'Économie Politique*, I., 145.

expiration of the period fixed for redemption to pay into the Federal Treasury an amount of coin equal to the face value of the notes still outstanding. The government then assumes the obligation of redemption for thirty years, after which the balance goes to a public fund. The Federal tax on circulation is one per cent. a year and the cantons are allowed to tax the average circulation of banks which are situated within their limits.[1]

The Swiss banking system as embodied in the law of 1881 is a system of free banking under government supervision. The Federal Assembly reserved the right to fix the aggregate of the Swiss circulation and to apportion it among the banks, but this right has been exercised only for the purpose of compelling the banks to conform to certain uniform requirements. Among these requirements, besides those already defined, are redemption of their notes in coin on demand and the acceptance at par of the notes of other specie-paying Swiss banks. The government in no way guarantees the circulation, except where the canton may be the owner of the bank, and the notes are not a legal tender in private contracts.[2] Twenty-six of the Swiss banks entered into a clearing arrangement by authority of a law of June 19, 1882, for the mutual exchange of notes. These banks are known as "The Associated Banks" (*Banques Concordataires*), and their notes circulate throughout Switzerland and are received by public depositaries.. The entire number of banks of issue in Switzerland is thirty-four, of which five operate under Articles 15 and 16 of the banking law. These articles permit the issue of notes against different forms of security from those required of the other banks, but do not dispense with the forty per cent. coin reserve.

The aggregate liabilities of the thirty-four Swiss banks on December 31, 1895, were 1,258,027,831 francs ($243,000,000), of which 196,200,000 francs was on account of circulation; 168,459,131 francs for current accounts and other short term obligatons; 649,132,940 francs for obligations at fixed terms;

[1] Comptroller's Report, 1895, Letter of Minister Brodhead, 104.
[2] Lévy, 216.

147,025,000 francs for paid-up capital; 27,483,163 francs for reserve fund; and the remainder for foreign bills, acceptances, and unpaid capital. The item of term obligations included 223,223,661 francs of savings bank deposits and 389,137,822 francs of deposit bonds and similar obligations. The assets included 77,339,580 francs in the legal specie reserve held against circulation; 16,003,595, francs "free" specie; 164,469,138 francs in domestic and 13,672,207 francs in foreign bills of exchange; 428,975,764 francs in advances; and 145,019,723 francs in public securities. The mean effective circulation outside the banks was 167,913,000 francs in 1895, against 158,719,000 francs in 1894. The maximum in 1895 was 185,146,000 francs in the week of November 9th and the minimum was 154,264,000 in the week of February 23d. The total cash reserve attained a mean during 1895 of 93,649,000 francs, of which 71,688,000 francs represented the forty per cent. reserve. The mean gold holdings were 82,667,000 francs and the mean silver 10,982,000 francs. The gold in 1894 was 77,190,000 and the silver 15,302,000 francs. The maximum cash reserve in 1895 was 98,417,000 francs in the week of January 26th and the minimum 90,461,000 francs in the week of October 5th.

The passion for a great state bank seized upon Swiss statesmen after the crisis of 1891 and an amendment was adopted to the constitution remitting to the Federal Council control of note issues.[1] The Chambers decided in favor of a state bank rather than a private joint stock bank, and the Department of Finance presented a project of law for the bank in the summer of 1894,[2] which yet remains to be put in operation. The first article declares the principal functions of the new bank to be to serve "as the regulator of the money market and to facilitate exchange operations." The principal seat is to be at Berne, but every canton has the right to demand the establishment of a branch

[1] The popular vote on the amendment was 228,853 in the affirmative and 143,939 in the negative. The amendment forbids forced legal tender except in time of war and exempts the bank from cantonal taxation.

[2] Raffalovich, *Le Marché Financier en 1894–5*, 167.

or agency within its own territory. The name of the new institution is to be "The Bank of the Swiss Confederation," the capital is to be furnished by an issue of bonds and the Confederation makes itself responsible for the engagements of the bank in case its own means prove insufficient. The capital is fixed at 25,000,000 francs ($5,000,000), but may be increased to 50,000,000 francs by vote of the Federal Assembly. "The exclusive right to issue bank bills" is conferred on the new institution and the existing banks are required to retire their circulation within two years and a half from the date when the new bank begins operations, by surrendering to the central bank quarterly one-tenth of the notes outstanding at that date. Deficiencies in the quota of notes must be made up in specie, to be held as a redemption fund for the retirement of the notes.

No fixed limit is put upon the note issues of the new bank, but it is required to hold gold coin or bullion or legal silver coins to the amount of one-third of the circulation. The Federal Treasury and the bank are alike required to accept bills at par and legal controversies relating to bank bills are to be tried before the Federal tribunals. Fifteen per cent. of the profits goes to the reserve fund, a proportion equal to four per cent. of the capital is paid as a dividend to the Confederation, and the remainder is apportioned, one-third to the Confederation and two-thirds among the cantons according to population. The new establishment is to be governed by a council board of twenty-one members elected for four years by the Federal Assembly and a committee of direction of from three to five members, appointed by the Federal Council.[1]

Banking in Spain.

Spain had banks of deposit during her period of prosperity in the Middle Ages, some of which, like that at Barcelona,[2]

[1] *Bulletin de Statistique*, November, 1894, XXXVI., 533–39.

[2] This bank, founded in 1401, is said to have been the first bank of deposit instituted for the accommodation of private merchants.—Hallam, II., 530.

attained considerable celebrity. These institutions disappeared with the decadence of Spanish commerce and it remained for the modern age to witness a new development of banking. An attempt was made in the eighteenth century to establish institutions of credit, and the Bank of San Carlos, which was founded in 1782 at Madrid, was still in operation when the monopoly of the issue of circulating notes was given to the Bank of Spain in 1874. The Bank of Spain was founded in 1829, under the name of the Bank of San Fernando, but did not enjoy any special privileges outside of Madrid and the places where it had branches until 1856.[1] It was at first a government bank and its name was changed at the time of the new legislation to the Bank of Spain, but even after 1856 the right to incorporate other banks of issue remained in the hands of the government. Such banks had been established prior to 1856 by the consent of the public authorities in much the same manner as departmental banks might have been established in France before 1840.

The legislation of January 8, 1856, was simply a first step in the direction of monopoly, like the similar legislation of France and Germany. This law prescribed that there should be not more than one bank of issue in any commercial city. The general provisions regarding the new banks limited their issues to three times their capital, obliged them to keep a coin reserve of at least one-third of their circulation, and fixed the minimum denomination of the notes at one hundred reals ($5). The liberality of these provisions was impaired by leaving to the government the nomination of the governor of the Bank of Spain and of royal commissioners to manage the independent banks. The Bank of Spain had created up to 1863 only two branches, at Valencia and at Alicanta, and there were independent banks at Cadiz, Barcelona, Seville, Malaga, Corunna, Santander, and Vallodolid. The capital of the independent banks was not large, but in this respect it was commensurate with the volume of business in Spain. The Bank of Spain on December

[1] Courcelle-Seneuil, 361.

31, 1862, showed a circulation of 208,380,901 reals ($10,400,000), a coin reserve of 107,398,201 reals, deposits of 235,063,731 reals, and a commercial portfolio of 309,231,378 reals ($15,500,000).

The charter of the Bank of Spain was extended in 1856 for twenty-five years and was renewed in 1874 for thirty years. The law of March 19, 1874, conferred upon the bank the exclusive privilege of issuing notes and increased the capital from 132,000,000 reals ($6,600,000) to 100,000,000 pesetas ($20,000,000).[1] All the existing provincial banks, then numbering eighteen, were ordered to liquidate their circulation and transfer it to the Bank of Spain. The bank is not a state institution and the state does not participate in its profits, but it had the authority, under the law of 1874, to require advances by the bank to the amount of 125,000,000 pesetas ($25,000,000) upon the deposit of proper guarantees. The notes of the bank were made legal tender and limited to five times the capital. The capital was increased soon after the Act of 1874 to 150,000,000 pesetas ($30,000,000), which carried the limit of circulation to 750,000,000 pesetas ($150,000,000).[2]

The necessities of the Treasury led to a new revision of the charter by the law of July 14, 1891, and the extension of the privilege of the bank until December 31, 1921. The new charter authorizes the issue of notes to the amount of 1,500,000,000 pesetas ($300,000,000) against a cash reserve of one-third, of which at least half is required to be kept in gold.[3] The bank was required to pay for these privileges by advancing 50,000,000 pesetas to the government annually for three years without interest or right to reimbursement until the expiration of the charter. The fate of the bank has come to be bound up more and more with that of the State and it has been only by the bank's help that the Treas-

[1] The present Spanish coinage system follows that of the Latin Union, the peseta being the equivalent of the franc ($0.193).

[2] Alfred Neymarck, Article, "Banque," in *Dictionnaire d'Économie Politique*, I., 140.

[3] *Bulletin de Statistique*, July, 1891, XXX., 72.

ury has been able to meet its engagements. The Treasury budget has shown a persistent deficit and a floating debt was incurred from 1885 to 1893 of 333,000,000 pesetas ($66,000,000). The permanent debt on June 30, 1892, was 6,249,639,975 pesetas ($1,200,000,000),[1] and the charges on account of the debt for 1894 were estimated at 309,219,669 pesetas ($61,000,000 or about $3.40 per capita). Exchange has declined about 20 per cent. and railway securities and public stocks have fallen from 15 to 75 per cent. during the past five years.

The commercial operations of the bank through its fifty-eight branches have become subordinate to the issue of paper notes to cover the advances to the state. A large proportion of the assets are locked up in government and foreign securities, which increased rapidly for several years because the bank maintained a uniform interest rate of four per cent., which afforded a profit upon the difference between this rate and the higher rate earned by the securities.[2] This difference was availed of by shrewd speculators to borrow on securities, spend the loan on new purchases of securities, deposit them again as guarantee for a larger loan, and so on without limit. The rate was raised in January, 1892, to five per cent., but without entirely curing the difficulty. The cash reserve, moreover, is only available for the redemption of notes to about half of its face value. The gold in the reserve on December 31, 1895, was 200,100,000 pesetas and the silver 275,550,000 pesetas. Gold is at a premium of 20 per cent. above bank-notes so that redemption in gold would immediately drain the bank. Redemptions are actually made in silver, whose present commercial value is below that of the bank paper. The Spanish peseta is the equivalent of the French franc, but five pesetas are required to obtain four francs, because of the greater stability of the French currency under the policy of restricted silver coinage and the fact that the franc is received as a token coin in the countries of the Latin Union at par with gold. The recent

[1] Raffalovich, *Le Marché Financier en 1893–4*, 217.
[2] Raffalovich, *Le Marché Financier en 1891*, 119.

insurrection in Cuba has required new appeals by the government to the bank and the circulation had been expanded on September 30, 1895, to 961,900,000 pesetas. The following table shows the principal items of the accounts of the bank since it acquired the monopoly of circulation:

DEC. 31st.	CIRCULATION.	CASH RESERVE.	COMMERCIAL BILLS.	ADVANCES.	CURRENT ACCOUNTS.
	(In millions of pesetas.)				
1875	127.7	129.1	15.1	41.0	87.1
1880	246.8	200.6	24.2	110.8	192.4
1885	469.0	272.2	74.4	188.3	234.1
1890	734.1	233.2	180.4	251.3	401.6
1893	934.0	375.0	342.7	135.1	374.3
1894	909.6	475.6	280.7	106.5	306.6
1895	987.0	475.1	356.4	——	384.7

The Bank of Portugal.

Portugal has a single public bank of issue with a capital of 13,500,000 milreis ($14,500,000). The statutes of the bank originally imposed careful restrictions on the circulation, but these restrictions have been suspended in order to permit large loans to the government which have tended to drag the circulation of the bank into the same mire of depreciation as the Bank of Spain. Article 15 of the original law prescribed that the circulation should always be covered by a metallic reserve and negotiable paper maturing in not more than three months and that the metallic reserve should be in gold and should equal one-third the aggregate of the circulation and other demand liabilities. Article 16 fixed the power of note issue at double the capital of the bank and Article 37 limited to 2,000,000 milreis the advances to the State.[1] Both the latter limitations have been disregarded and the circulation is now four times the capital and advances to the government are more than ten times the amount fixed by law.

The last extension of the charter continued the bank for forty years, from 1888 to 1928, and conferred upon it the

[1] Lévy, 208.

monopoly of the issue of legal tender notes in the realm of Portugal and the neighboring islands. Seven other banks, five at Oporto, one at Braga, and one at Guimaraes, had the power to issue notes for circulation within their respective districts, which were not received by public depositaries. An arrangement of July 8, 1891, authorized the Bank of Portugal to unify the circulation and substitute its own notes for those of the other banks. The bank is managed by a governor appointed by the Treasury for three years and a board of ten directors chosen by the shareholders. The accounts of the bank on September 30, 1895, showed a note circulation of 55,000,000 milreis ($59,000,000), protected by a specie reserve of 12,400,000 milreis, of which only 4,850,000 milreis ($5,250,000) was in gold and 7,550,000 milreis ($8,150,000) in silver. The commercial portfolio amounted to 11,300,000 milreis and the current accounts to 1,300,000 milreis.

The Banks of Greece.

Greece has three banks of issue,—the National Bank of Greece, founded in 1842; the Ionian Bank, founded in 1839; and the Epiro-Thessalian Bank. The capital of the National Bank is 20,000,000 drachmas. The Ionian Bank has its head office in London and its paid-up capital is £315,507, or 7,887,687 drachmas.[1] All three banks have been dragged into the channel of forced legal tender and depreciated money by the enormous debts of the government and the steadily growing embarrassments of the public Treasury. A law of June 20, 1877, gave forced legal tender quality for the first time in recent years to the notes of the National Bank to a limit of 47,000,000 drachmas ($9,071,000) and to those of the Ionian Bank to a limit of 12,000,000 drachmas ($2,316,000). The money was restored to par in 1884 at a heavy expense

[1] The coinage systems of Greece, Roumania, Bulgaria, and Servia are each based upon the French decimal system and their monetary unit in gold, though having different names, is equivalent to the franc, which is valued by the United States Mint at nineteen and three-tenths cents ($0.193.)

to the Treasury, but the suspension of specie payments was thought necessary again in October, 1885, and authority to issue inconvertible notes was extended to the Epiro-Thessalian Bank as well as to the other two banks. The National Bank was authorized to issue notes of which one-third should be covered by coin and bullion, one-third by commercial paper, and one-third by securities. The government borrowed from the bank 14,000,000 drachmas in gold and required it to hold notes subject to its orders to the amount of 70,000,000 drachmas. The bank was given in return for these advances the right to circulate 60,000,000 drachmas on its own account in inconvertible paper. The Ionian Bank was authorized to maintain a circulation of 7,000,000 drachmas, of which 2,000,000 should be on account of the government, and the Epiro-Thessalian Bank was given a maximum circulation of 5,000,000 drachms, of which 800,000 should be on government account. The National Bank was also authorized to circulate 7,000,000 drachmas in small notes, and each of the other banks was authorized to issue 3,500,000 drachmas in such notes. The metallic reserve of the National Bank has been reduced below 2,000,000 drachmas ($400,000) and while gold sometimes reaches the country after the sale of the crops it quickly flies abroad again or disappears into private hoards. The price of gold in paper was 122 in 1889 and 1890, 140 in 1892, 180 in 1893, and 200 in 1894.[1]

The population of Greece is about 2,300,000, and the annual budget for carrying on the government averages about 100,000,000 drachmas ($20,000,000), of which 35,000,000 drachmas is on account of interest on the debt. This interest has not been paid for several years in gold, as required by the contract, but desultory efforts have been made to persuade the holders of the securities to accept new securities in payment of interest or to permit a complete readjustment of Greek finances. The British holders of Greek securities persuaded the London Foreign Office in 1892 to send Major

[1] Raffalovich, *Le Marché Financier en 1893–4*, 231.

Law to Athens to study the actual condition of affairs and to determine whether the government would be able to meet its obligations. Major Law made a report to the British minister at Athens under date of March 10, 1893, recommending various reforms in the financial system. He showed that the aggregate public debt on January 1, 1893, was about 750,000,000 drachmas ($150,000,000 or about $60 per head). Greece imports more than she exports and the accumulated deficits in the annual budgets since 1877, due to the premium on gold and the inefficient methods of collecting the revenues, have been 674,000,000 drachmas.

Major Law's recommendations were not adopted and no definite plan has yet been perfected for the restoration of order to Greek finance. The King, in his speech from the throne on November 8, 1893, afforded striking evidence of the depreciation of the bank-notes and the evils which have come in its train. It was announced that all the subsidiary coins, even to those of bronze, had disappeared and the government recommended the coinage at Paris of nickel pieces of five, ten, and twenty centimes to supply the people with small change. A law was approved December 1, 1893,[1] providing for the payment of 50 per cent. of the interest then overdue on the public debt in bank-bills, for future payments in the proportion of 30 per cent. in gold, and for covering directly into the Treasury certain funds which had been pledged as the guarantee of particular loans. This legislation led to protests by the European bond-holders and several abortive efforts to readjust the debt. Meanwhile, values in Greece have shrunk 225,000,000 drachmas, the gold drachma has risen to 200 per cent. in paper, high prices and an excess of paper circulation have failed to stimulate exports, and raisins, the principal article of export, have been shut from France and their export to the United States has been reduced by the high tariffs which those countries have established.[2]

[1] The Greeks still adhere to the Julian calendar. The actual date by the Gregorian calendar, in use in Western Europe, was December 13th.

[2] Raffalovich, *Le Marché Financier en 1894–95*, 282–84.

One of the essential defects of the Greek banking system is the large proportion of assets required to be locked up in mortgages. The law requires three-fourths of the capital of the National Bank and three-fourths of the capital and reserve funds of the Epiro-Thessalian Bank to be thus invested. The English bank is free from these restrictions. The government is not a shareholder in either of the banks, but appoints a royal commissioner to supervise the operations of each and requires the publication of periodical reports. The banks pay a tax of five per cent. on their dividends and the customary house-tax, and transfer public monies free of charge.[1] The shareholders are liable only for the amount of their investment. The National Bank has twenty-six branches and the others have several each.

The manner in which the resources of the National Bank have been absorbed by the government and by mortgage investments is indicated in a striking manner by the balance sheet for October 1, 1895. The total liabilities were 247,253,095 drachmas (about $47,700,000 in nominal gold value, but about half this amount in silver or paper). These liabilities comprized 106,252,864 drachmas in circulating notes, 7,000,000 drachmas in small notes, 94,727,724 drachmas in deposits and current accounts, 11,500,000 drachmas on account of reserve fund, and the remainder on account of capital and other smaller items. The resources for meeting this mass of liability included 1,852,396 drachmas in cash, 2,965,500 drachmas in the notes of other banks, 8,938,462 drachmas in foreign credits, 10,430,598 drachmas in advances to the government, 38,487,457 drachmas in government bonds, 28,435,445 drachmas in sundry loans to public bodies, 38,818,548 drachmas in advances on first mortgages, 77,787,754 drachmas on forced currency and notes of one and two drachmas, and only 12,091,897 drachmas,—or about one-twentieth part of the assets,—in unmatured commercial bills.

The condition of the Ionian Bank more nearly conforms

[1] Letter of Minister E. Alexander, Comptroller's Report, 1895, 84.

to sound banking principles. The total liabilities on September 1, 1895, were 33,763,979 drachmas, of which 7,887,687 drachmas was on account of capital, 8,566,061 drachmas was for circulation, 3,495,298 drachmas for small notes, 3,831,876 drachmas for current accounts, and 8,150,292 drachmas for interest-bearing deposits. The assets included 402,578 drachmas in cash on hand, 230,874 drachmas cash in London, 1,362,822 drachmas in notes of other banks, 3,670,668 drachmas in investments in London, 5,412,908 drachmas in commercial bills, 10,463,647 drachmas advanced on securities and mortgages, 3,894,280 drachmas in loans to the government on forced currency, and 3,499,999 drachmas in loans on small notes.

The Imperial Ottoman Bank.

The Imperial Ottoman Bank at Constantinople received the exclusive privilege of note issue in Turkey when it was founded in 1863. The capital was furnished by British and French capitalists and was originally £2,700,000. This was increased in 1865 to £4,050,000 and in August, 1874, by the absorption of the Austro-Ottoman Bank, to £10,000,000, of which half has been paid up.[1] The first charter was for thirty years, but a new convention of February 17, 1875, prolonged the privileges of the bank for an additional period of twenty years, until 1913. The bank is required to maintain a cash reserve equal to one-third of its circulating notes and these notes must be paid in coin to the bearer on presentation. They are a legal tender in the districts in which they are issued and where the branches of the bank are established. The government is pledged by the charter to issue no paper money during the continuance of the bank and to authorize the creation of no other bank or establishment with like privileges. The notes of the bank are receivable at public depositaries and a large part of its functions relate to its duties as financial agent of the Turkish government. A new convention was concluded with the

[1] *Revue des Banques*, May, 1895, XIV., 100.

government for a period of six years in 1893, for the purpose of regulating the advances by the bank to the Treasury. The maintenance of a floating debt is a necessary feature of the present methods of taxation in Turkey, as most of the revenue is obtained by a levy upon the land and crops and is not paid until after the crops are harvested.[1] The advances to the government are largely reimbursed when the taxes are collected. The total advances on January 1. 1895, were £1,358,927.

The Turkish people have not yet become large users of bank-notes and are easily excited to distrust. This happened in the summer of 1894, when some forged notes were found in circulation and the public presented £218,000 for redemption within a week. The circulation at the head office, which was £249,000 during the first week in June, fell to £66,000 during the first week of July. The circulation of the bank was as high as £990,000 in 1893, but was only £838,797 at the close of 1894. The experience of this run taught the management the importance of maintaining a strong coin reserve and prepared them for the run which set in during the political disturbances growing out of the Armenian massacres in the autumn of 1895. The government offered the bank the privilege of suspending specie payments for thirty days, but the offer was declined and £1,300,000 in gold was obtained early in November from the Bank of France. The Imperial government were so pleased with the spirit shown by the bank that the charter was extended for twelve years, until 1925.[2] The cash in hand at Constantinople and the branches was £1,746,905 on January 1, 1895, and £1,907,000 on July 31, 1895. The bank also held English and French government securities on January 1, 1895, to the amount of £1,510,007.

The bank has been extending its branches of late years and has been finding them more profitable as their convenience to commerce has come to be understood. Branches exist at

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[1] Lévy, 227.

[2] London *Bankers' Magazine*, Dec., 1895, LX., 726.

Smyrna, Bagdad, Aleppo, and Alexandria, and those at Smyrna and Bagdad showed a material increase of business during 1893 and 1894. The number of branches rose from fourteen in 1883 to twenty-eight in 1894, and an encouraging feature of this development has been the fact that increased advances of capital by the parent bank have not been required at the branches in proportion to the increasing volume of business, but the capital has been furnished by the communities.[1] The growth of deposits has also been an encouraging feature of the history of the bank, the amount having increased from about £8,000,000 of all classes in 1893 to £8,556,469 in current accounts and £1,427,196 for fixed terms on January 1, 1895. The private securities held, representing the commercial portfolio, were £3,492,847; the advances on securities were £4,920,796; and the current accounts of sundries were £4,679,364. Business conditions were not favorable in Turkey during 1894, but some conversions of the public debt and other large financial transactions enabled the bank to show net profits of £457,840 and to pay a dividend of eight per cent.

The Banks of Roumania, Bulgaria, and Servia.

The National Bank of Roumania was founded in 1880 with the exclusive privilege of issuing notes payable to bearer until December 31, 1912. The capital is 30,000,000 lei ($6,000,000) of which 12,000,000 lei have been paid in. A third of the capital is furnished by the government and the other two-thirds by individuals. A metallic reserve of at least one-third of the note issues is required and no bill can be issued below twenty lei ($4). The entire circulation must be covered by securities which are readily negotiable, but thirty per cent. of the metallic reserve may be represented by foreign bills of exchange.[2] The circulation on Sep-

[1] London *Bankers' Magazine*, Aug. 1895, LX., 252.

[2] Lévy, 225. The gold standard was adopted in Roumania by the law of March 2, 1890. The unit in the three Slavic countries is the equivalent of the French franc ($0.193).

tember 30, 1895, was 139,900,000 lei ($27,000,000), the gold reserve was 63,700,000 lei, and the foreign drafts were 9,700,000 lei. The domestic discounts were 21,900,000 lei; advances, 17,800,000 lei; and current deposit accounts, 10,200,000 lei. The government of Roumania issued paper money soon after its establishment in 1878, guaranteed by the public domains to the amount of 26,200,000 lei, and the National Bank was charged with the withdrawal of this paper and the substitution of its own notes. The amount of this special issue has been gradually retired and the bank reimbursed by the government until it has disappeared. The net profits of the bank in 1894 were 3,203,000 lei.[1]

The bank-note circulation of Bulgaria is issued by the National Bank, which was founded on February 8, 1885, by the government, with a capital of 10,000,000 lei ($2,000,000) in gold. The bank has the exclusive privilege of issuing notes, and they are received in the public depositaries and in all other offices of the government. It is required to hold a cash reserve in gold equal to one-third the value of the notes in circulation and to redeem the notes on demand at the central office or at any of the branches. The governor of the bank is named by the Prince upon the nomination of the Minister of Finance and four administrators are appointed in the same way. The government is represented by two delegates, one a counsellor of the court of accounts and the other a member of the ministry of finance, who exercise official supervision over the operations of the bank. The circulation of the bank on July 14, 1895, was only 2,300,000 levs ($444,000), the cash reserve was 4,100,000 levs, the portfolio of commercial paper 19,300,000 levs, and the current accounts 40,900,000 levs.

The bank-note circulation of Servia is issued by the National Bank of Servia, which was established by the law of January 6, 1883, subsequently modified by the law of September 23, 1885. The capital of the bank is 20,000,000 dinars ($4,000,000). The privilege of the bank is fixed

[1] *Revue des Banques*, April, 1895, XIV., 71.

for twenty-five years and includes the monopoly of note issues. The notes of ten dinars ($2) are redeemable in silver and those of larger denominations in gold. The bank is authorized, however, to redeem in silver at its market value in a proportion fixed by the Minister of Finance upon the special petition of the bank. Silver may also be substituted for gold to the amount of not more than twenty-five per cent. of the cash reserve and the bank is not permitted to increase its note issues above two and a half times its reserve. The provision that the notes may be redeemable in part in silver has led to a degree of distrust of the note issues somewhat similar to that which existed in 1893 in the United States regarding the notes issued under the Sherman law. The distrust went far enough in Servia to send gold to a premium, in spite of the fact that the bank offered to pay 100 francs in gold for 115 francs in silver or in notes redeemable in silver. This did not accord with the market value of silver, but it was feared that the gold reserve of the bank would become exhausted and that gold payments would be suspended. The circulation of the bank on September 22, 1895, was 26,600,000 dinars ($5,134,000), protected by a specie reserve of 10,800,000 dinars, of which 6,100,000 dinars was in gold and 4,700,000 dinars in silver. The discounts were 7,900,000 dinars, and current accounts 1,500,000 dinars.

CHAPTER XIII.

THE BANK OF THE UNITED STATES.

Banks of Issue before the Adoption of the Constitution—Hamilton's Plan for the First Bank of the United States—The Struggle over a New Charter—The Second Bank of the United States: Its Early Errors and its Economic Services—The Bank Dragged into Politics by Jackson and Clay—Jackson's Triumph and the Removal of the Deposits—The Independent Treasury System.

THE pathway of American colonial history is thickly strewn with the failures of government paper money, which might have afforded an instructive lesson to the Continental Congress against its issues of Continental bills. Several cases are found also of issues on private banking credit, but they were not based on sound banking principles and do not shine greatly by comparison with the unrestrained issues resting on the fiat of the State. The "Land and Manufactures Bank," established in Massachusetts in 1740, did not pretend to do better than issue notes redeemable in goods, but they stood for a time so much higher than "Massachusetts bills" that, in spite of the hostility of Governor Belcher, merchants specially advertised goods to be sold for "Manufactory bills."[1] In Connecticut in 1733 the New London Society for Trade and Commerce circulated notes which were current until prohibited by the authorities, and in New Hampshire a company of "private gentlemen" attempted to meet the demand for a circulating medium by an issue of bills. Most of these schemes, including that of the specie bank, formed to counteract the

[1] Weeden, 487.

Land and Manufactures Bank, fell under the prohibition of the Joint Stock Companies' Act. This act was passed in England after the bursting of the South Sea Bubble in 1720 and forbade the formation of banking companies without a special charter, but it was not until 1740 that it was declared by Parliament to extend to the colonies.

The history of banks of issue in the United States can hardly be said to have begun, however, until the foundation of the Bank of Pennsylvania. The bank originated in the plan of a number of citizens of Philadelphia to supply the army with rations, and their first bills, issued in 1780, were nothing more than interest-bearing notes payable at a future time. The advances in Continental money made by the shareholders were secured by bills of exchange for £150,000 drawn on the envoys in Europe, but not intended to be negotiated.[1] Approval was given by Congress May 26, 1781, to the plan of Robert Morris for the Bank of North America, with a capital of $400,000, to be increased if desired. Morris arranged with the Bank of Pennsylvania to transfer the foreign bills it was holding to the new bank and paid in cash its claims against the Federation. The charter of the Bank of North America was not actually granted until December 31, 1781, and business was begun January 7, 1782. There was so much doubt of the power of Congress to charter a bank that a charter was obtained April 1, 1782, from the State of Pennsylvania, under which the bank continued to operate until absorbed into the national banking system in 1863. The bank did much to restore order to the chaos of Federation finances and loaned Morris, as Superintendent of Finance, $1,249,975, of which $996,581 was repaid in cash and the remainder by surrendering the bank stock owned by the Federation. The government had originally paid for its stock in silver brought from France, but this silver was infinitely more productive by the skilful management of the bank than it could ever have been if covered into the public treasury. Livingston wrote to Dana December 17, 1782:

[1] Sumner, *Finances of the American Revolution*, II., 22.

Paper is entirely out of circulation, if we except the bank paper, which, being payable at sight in specie, is equal to it in value. So extensive has this circulation been that the managers not long since published a distribution of the first *half-year's* dividend at four and a half per cent. notwithstanding a variety of expenses to which they had been put in the first organization of the bank.[1]

The first Bank of the United States was incorporated by the First Congress in 1791,[2] as a part of the scheme of Alexander Hamilton to strengthen the new Federal government. Those who had opposed the adoption of the Constitution because of its centralizing tendencies, and some of those who had supported it, opposed the granting of the bank charter upon the ground that the Constitution contained no express grant to Congress of the power to establish a corporation. Their argument was that the case fell plainly within the rule subsequently embodied in the tenth amendment to the Constitution, that "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively or to the people." President Washington obtained the opinion of the members of the cabinet before signing the bill. The opinions of Jefferson and Edmund Randolph were adverse to the constitutionality of the measure; but Washington followed the advice of Hamilton, his brilliant young Secretary of the Treasury, and gave the bill his approval.

The capital of the Bank of the United States was fixed at $10,000,000, divided into 25,000 shares of $400 each. The protection of small investors in bank stock was sought by a graduated scale of voting which did not permit more than thirty votes to any shareholder. Foreign shareholders were not allowed to vote by proxy, which practically prevented their voting at all. The number of directors was fixed at twenty-five, who must be citizens of the United States and not more than three-fourths of whom were eligible for re-election. The bank was not forbidden to loan on real estate security, but could not become an owner of real estate

[1] Wharton, *Diplomatic Correspondence*, VI., 146.

[2] Act of February 25, 1791.

(beyond what was needed for banking houses) unless the property came into its hands in satisfaction of mortgages or judgments.[1] The only limitation upon note issues was that which limited all debts other than deposits to the amount of the capital stock. The notes were receivable for dues to the government so long as they were redeemable in coin on demand. The charter was granted for twenty years, with the provision that Congress should not charter another bank within that time. This was far from implying a monopoly of note issues, for the State banks were in no way disturbed in their privileges and methods except so far as the new institution by its example acted as a regulator of the currency. Its large capital and pre-eminent position operated, and were intended to operate, to give it such a commanding position as was occupied by the Bank of England among the country banks of that country.

The charter provided that one-fifth of the capital should be subscribed by the government of the United States, but a loan was to be made to the government equal to the amount subscribed, to be repaid in ten annual instalments of $200,000 each, with interest at six per cent. No other loans were to be made to the government exceeding $100,000 without authority of law. The practical effect of the government holdings of stock was simply to give the bank the note of the government for its final payment, but as the bank was forbidden to deal in its own stock the process of issue of the government stock was somewhat complicated. It would have been useless for the government to draw money from Europe to pay into the treasury of the bank, to be immediately drawn out again and remitted to Europe for charges there. The course adopted was for the Treasurer of the United States to draw bills of exchange on the American Commissioners in Amsterdam for the amount required to

[1] It is significant of Hamilton's growing familiarity with finance that he did not revive the project of the bank of issue based upon landed security which had attracted him a few years before, but laid down in his report the correct theory of a credit currency based upon quick assets.—*Works*, III., 106–107.

pay the bank. The bills were purchased by the bank and warrants issued in favor of the Treasury upon the bank, thereby placing the amount in the Treasury. Other warrants were then issued upon the Treasury in favor of the bank for the amount of the subscription to the stock, which the bank receipted for as paid. The stock having been thus paid for in accordance with law, the bank loaned $2,000,000 to the government in accordance with the act of incorporation by handing over the bills of exchange originally drawn by the Treasury on Amsterdam.[1]

The Bank of the United States was authorized to establish offices of discount and deposit in the several States and $4,700,000 of the capital was reserved for the central bank at Philadelphia. The remainder was divided among eight branches, established eventually at New York, Baltimore, Boston, Washington, Norfolk, Charleston, Savannah and New Orleans. Private subscriptions were required to be paid one-fourth in gold and silver and three-fourths in six per cent. government stocks or in three per cent. stocks. The capital was over-subscribed to the amount of four thousand shares within two hours after the opening of the books. Oliver Wolcott, who afterwards succeeded Hamilton as Secretary of the Treasury, was offered the presidency, but declined, and Thomas Willing of Philadelphia was selected.

The bank was more successful in its commercial dealings than in obtaining prompt payment of its advances to the government. No regular reports were made to the Treasury Department, but the report communicated to Congress by Secretary Gallatin for January 24, 1811, showed resources of $24,183,046, of which the leading items were $14,578,294 in loans and discounts, $2,750,000 in United State six per cent. stock, and $5,009,567 in specie. The leading items of liability were $10,000,000 on account of capital, $5,037,125 in circulating notes, $5,900,423 in individual deposits, and $1,929,999 in United States deposits. The average annual dividends paid up to March, 1809, were over eight per cent.

[1] Bolles, II., 129-30.

The bank made several loans to the government in anticipation of the revenues early in its career. They were not promptly paid and the debt of the government to the bank at the end of 1792 was $2,556,595, which increased at the end of 1795 to $6,200,000. An attempt was made to sell government five per cent. stock, but only $120,000 was realized and it became necessary for the government to part with one of its most valuable assets,—its shares in the bank. The third and fourth instalments of the original $2,000,000 loan to the government were not paid until 1797, when 2160 shares of the government stock were sold at $500 per share (a premium of $100) and the proceeds, $1,080,000, were applied to these two instalments and to other obligations of the government to the bank. Six hundred and twenty more shares were sold soon afterwards for $304,260 and in 1802 the remaining shares were sold at an advance of forty-five per cent. and the government ceased to be a stock-holder. Secretary Gallatin reported in 1809 that the government made a profit of $671,860 on the sale of its shares, besides receiving dividends at the rate of about eight and three-eights per cent. annually. The aggregate payments by the government, including interest, were $2,636,427, while the proceeds and dividends together were $3,773,580, representing a profit of nearly fifty-seven per cent. on the original investment for the eleven years during which the government was a shareholder.[1]

Opposition to the Bank of the United States did not die out with Washington's administration nor with its large advances to the government. The conception of the functions of a bank which then prevailed is indicated by President Jefferson's letter of July 12, 1803, to Gallatin, in which he declared, "I am decidedly in favor of making all the banks republican by sharing deposits among them in proportion to the dispositions they show." The bank had a steady friend in Gallatin, however, and he not only continued to avail himself of its assistance in the fiscal operations of the

[1] Sen. Ex. Doc. 38, 52d Cong., 2d Sess., 34.

government, but induced Jefferson to approve a bill establishing a branch at New Orleans.

The charter of the bank was to expire in 1811 and the shareholders petitioned in 1808 for a renewal. The proposal was strongly supported by Gallatin in a report of March 9, 1809, reviewing the entire history of the bank. He recommended that the capital be increased to $30,000,000, with a view to lending three-fifths of the amount to the government in case of war, and that the States be allowed to subscribe $15,000,000. The advantage derived by the government from the existing bank he classified under the four heads of safe keeping of the public monies, transmission of public monies, collection of revenue, and loans.[1] Congress was not disposed to adopt so comprehensive a scheme as this, but theoretical opposition to the bank had so far yielded to practical considerations that the terms of a contract were arranged for a new charter, which received the approval of the House on April 21, 1810, by a vote of 75 to 35. It was the fatal incapacity of the Eleventh Congress to take positive action which prevented the taking up of the bill again, and gave the State bankers time to organize an opposition and instruct their senators against re-charter.[2]

The charter was opposed at the next session not only by the advocates of strict construction of the Constitution, but by party factions opposed to Gallatin in the Cabinet and the Senate. William Duane and Michael Leib had attempted to dictate the Federal appointments in Philadelphia and upon Gallatin's refusal to submit became his bitter enemies. They were supported in the bank contest by a Maryland clique headed by Robert Smith, the Secretary of State, and Senator Samuel Smith, his brother. The fact that about 1800 of the 2500 shares were held abroad was made the occasion of bitter attacks upon the bank. A type of this sort of opposition was the speech of Mr. Desha of Kentucky, in the House on February 12, 1811, in which he declared that this accumulation of foreign capital was one of the engines for

[1] Stevens, 261.
[2] Adams, V., 208.

overturning civil liberty and that he had no doubt George III. was a principal stock-holder and would authorize his agent in this country to bid millions for a renewal of the charter.[1] Gallatin had anticipated this ground of hostility in his report to Congress. He called attention to the fact that the foreign shareholders had no vote and that if the charter was not renewed the principal of the foreign holdings would have to be remitted abroad in liquidation of the affairs of the bank.

William H. Crawford of Georgia was the champion of Gallatin and the bank in the Senate and his able argument commended him to the administration and made him a strong candidate in later years for the presidency. Henry Clay held that Congress had no power to create the bank or to continue it, and followed the leanings of Mr. Desha in the opinion that in case of war with England "the English premier" would exercise control over the institution. The House on January 24, 1811, postponed indefinitely the bill for renewing the charter by a vote of 65 to 64. The vote in the Senate on February 20th was 17 to 17, and the Vice-President, George Clinton, an enemy of Gallatin, gave the casting vote against the bill. "The necessity for such an institution," says Mr. Henry Adams, "was merely one of the moment, but in the period of national history between 1790 and 1860, the year 1811 was perhaps the only moment when destruction of the bank threatened national ruin."[2] The government was compelled to rely in the war of 1812 on the State banks, and their suspension of specie payments in 1814 almost paralyzed the operations of the Treasury. It became impossible to make transfers of funds from one part of the Union to another, because the notes of the banks of one section did not pass current in other sections. Gallatin has left on record the opinion that the suspension of specie payments in 1814 "might have been prevented at the time when it took place, had the former Bank of the United States been still in existence." He believed that the bank would have

[1] White, 265.

[2] *History of the United States*, V., 329.

aided the treasury and that "both acting in concert would certainly have been able at least to retard the event; and, as the treaty of peace was ratified within less than six months after the suspension took place, that catastrophe would have been altogether avoided."

The necessity for means of carrying on the war with Great Britain led to a great variety of odd proposals in Congress after the suspension of 1814. One of the crudest of these was a plan of ex-President Jefferson's, communicated to President Madison, to issue $20,000,000 in government promissory notes annually as long as might be necessary and to appeal to the State legislatures to relinquish the right to establish banks. Dallas, who succeeded Gallatin as Secretary of the Treasury on October 6, 1814, indicated indirectly his opinion of this scheme by recommending a new bank and remarking that "The extremity of that day cannot be anticipated when any honest and enlightened statesman will again venture upon the desperate expedient of a tender law."[1] The plan of Dallas, as set forth in his report of October 17th, was for a bank with a capital of $50,000,000, empowered to lend $30,000,000 to the Treasury. There was a provision in the bill reported, authorizing the suspension of specie payments at the discretion of the President of the United States, and it was fallen upon by Daniel Webster in a speech of great power and eloquence. He urged the creation of a bank for commercial purposes rather than one involved at the outset with the government. The result of his attack was the defeat of the bill by a tie vote, which was then reconsidered and the bill sent to a select committee. Amendments were adopted which met Mr. Webster's views, but in this form the measure did not meet the wants of the Treasury. It passed the House, 120 to 38, and the Senate, 20 to 14, but was vetoed by the President on January 30, 1815. Another effort was made to pass the Dallas bill, but it failed in the House on February 17th by a majority of one vote.

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[1] Adams, VIII., 245–49.

The evils of the currency had not been remedied when Congress met again in December, 1815, and President Madison suggested a national bank as a suitable instrument for promoting specie payments. Secretary Dallas submitted a detailed plan for the bank, which was adopted by Congress with little change. The capital of the new bank was fixed at $35,000,000, of which one-fifth was to be subscribed by the government in money or in its own obligations. The government subscription was by a stock note, which was not fully paid up in cash until 1831. The public funds were to be deposited in the bank, "unless the Secretary of the Treasury shall at any time otherwise order and direct; in which case the Secretary of the Treasury shall immediately lay before Congress, if in session, and if not, immediately after the commencement of the next session, the reasons for such order or direction." Twenty-five directors were to be chosen, five to be named by the President, and the notes of the bank were made receivable in all payments to the United States. The bank was again given duration for twenty years and no other bank was to be established within this time by Congress outside the District of Columbia. This privilege, as in the case of the first bank, carried with it no restrictions upon the State banks of issue except such as the new bank was expected to exercise by its moral and financial influence towards the restoration of specie payments. A bonus to the government was required of $500,000 annually for three years after the end of the second year.

The progress of public opinion in favor of the implied powers of the Federal government under the Constitution is indicated by the attitude of Madison and the democratic party towards the incorporation of the second Bank of the United States. Madison as a member of the First Congress had opposed the incorporation of the Bank of the United States upon constitutional grounds, and in 1799 had alluded to it as one of the examples of the usurping tendencies of the Federal government;[1] but as President in 1814 and 1815

[1] Von Holst, I., 388.

he was willing to treat the constitutional issue as *res adjudicata*. More surprising is the fact that Calhoun, in later years the hair-splitting logician of strict construction and the champion of nullification, was found foremost among the supporters of the charter of the second bank. He reported the bill to the House and suggested that if the bank by its financial policy was unable to compel the State banks to return to specie payments, Congress might resort to stronger measures, which were within their power. Both Calhoun and Webster favored the refusal by the government of the notes of suspended banks and the collection of all government dues in specie.[1] Webster secured an amendment to the bank bill, requiring the payment of deposits as well as notes in specie, subject to a forfeit of twelve per cent. on the amount for which specie payment was refused.

The constitutional question had thus been decided by the legislative branch of the government before it reached the Supreme Court in 1819. That court, in the celebrated case of McCulloch vs. Maryland, in which the decision was rendered by Chief-Justice Marshall, decided that the power to create a national bank, to assist in carrying on the fiscal operations of the government, was within the implied powers of the Constitution. Equally important was the decision upon the direct issue raised in that case, whether the States could constitutionally levy taxes upon the circulating notes or the property of a national bank. Representative Fiske of New York, in a strong speech in favor of the renewal of the first charter in 1811, declared that the States, in order to give the preference to their own paper, might exclude that of any other State from circulation within their limits by taxation.[2] He did not suggest that they might pursue the same policy towards the notes of a national bank, but this position was taken by the State of Maryland towards the notes of the second Bank of the United States, and the case was carried to the Supreme Court. A decision in favor of the right of the States to have taxed the circulating notes of

[1] White, 278.
[2] Bolles, II., 150.

the United States or of corporations chartered under its laws, would have precluded forever the creation of a national currency, issued either by the government or by national banks. Indeed, if the Federal government had not the power to withdraw its creations from discriminating legislation by the States, Chief-Justice Marshall declared, they might tax the mail or the mint, the papers of the custom house, or the forms of judicial process.[1]

The question of the existence of the bank in the face of discriminating State taxation was not an academic one in 1818 and the following years, but one which was severely practical. The efforts of the bank to drive the State notes from circulation, and especially its later contraction of discounts when it found itself on the verge of bankruptcy, caused commercial distress and made the bank exceedingly unpopular. North Carolina laid a tax of $5000 per year on the branch at Fayetteville. Kentucky, Tennessee, Ohio, and Maryland laid taxes on circulation or on the branches as such. The Maryland act required the purchase of stamped paper for the printing of the circulating notes or the annual payment of $15,000 by the branch at Baltimore. The branch continued to issue notes on unstamped paper and the cashier, William McCulloch, was sued for debt and gave his name to one of the most celebrated of American constitutional cases.[2] Chief-Justice Marshall, in rendering his decision, admitted that the States possessed unimpaired the power of taxing the people and property of the State and that it might tax the real property of the bank in common with other such property within the State, and might tax the interest of citizens of Maryland in the bank; but he declared that the Constitution of the United States placed beyond the reach of State power all the powers conferred on the government of the Union and all the means given for the purpose of carrying those powers into execution.[3]

[1] 4 Wheaton, 316.

[2] McMaster, IV., 497.

[3] Following this decision, all securities of the United States have been held free from taxation by the States unless with the consent of

The Bank of the United States was badly managed during the first years of its existence and in the summer of 1818 was upon the verge of insolvency. The bank began business January 7, 1817, and violated its charter from the outset. The proportion of specie required to be paid in on the second and third instalments was not paid and the bank loaned money to stockholders on the pledge of their stock and personal notes. Trading in shares before they were paid for pushed up the quotations and the bank loaned on the increased value when other nominal security was furnished in the form of mutual indorsements. The Baltimore branch was practically wrecked by its managers, with a loss of $1,671,221. The policy adopted for restoring specie payments was also defective. An arrangement was made with the leading banks of New York, Philadelphia, and Richmond for the resumption of specie payments by them on February 20, 1817. The public deposits in these banks, which the government had been unwilling to accept in depreciated bank paper, were to be transferred to the Bank of the United States, but checks on the State banks which were parties to the agreement received by the Bank of the United States were to be credited as cash. Arrangements were also made for liberal discounts by the new bank, in order to relieve the local banks from the commercial pressure.

These features of the resumption policy were not subject to criticism and $7,472,419 in public funds and $3,336,491 in special deposits were transferred from the State banks to the

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the United States. The national banks created under the Act of June 3, 1864, for many years availed themselves of this condition to have as large a proportion of their reserves as possible in United States notes at the times when their property became subject to assessment for taxation under State laws. This practice led to an act of Congress in 1894, authorizing the States to tax such notes at the same rate as other money. It was long held that the instruments of State sovereignty were exempt from Federal taxation upon the same grounds that the instruments of Federal sovereignty were exempt from State taxation, but this view was overruled in regard to the circulating notes of State banks in the case of Veazie Bank *vs.* Fenno, 8 Wall., 533. See Kent, I., 429, note.

central bank at Philadelphia. Eighteen branches of the Bank of the United States were established and the notes issued were received for government dues without reference to the place of issue and were redeemable, wherever issued, by the central bank or any of its branches. The mistake made by the new bank was in directing the branches to push their own notes into circulation in place of those of the State banks, and to issue drafts on the Eastern cities to prevent the remittance of their own notes. The notes of the local banks were locked up in the Bank of the United States and interest charged upon them to the local banks, but both the notes of the branches and the branch drafts were remitted eastward by the operations of trade. The notes of the Western branch banks which were remitted to the East thus exercised no controlling influence over the volume of Western business, for they were not presented for redemption in the West. What made the matter worse was the necessity imposed in many cases on the branches, in view of the eastward movement of their own notes, to pay out again the local notes in the granting of discounts.

The Western branches paid but limited attention to the instructions of the parent bank to diminish their discounts, even after the danger of their policy became apparent. They issued what were known as "race-horse bills," by which drafts were made by one branch upon another, which were met when due at the accepting bank by new drafts upon some other branch. The bank imported $7,311,750 in specie from Europe during its first two years at a cost of $525,247,[1] but the drain upon its resources had reduced the specie in Philadelphia on April 21, 1819, to $126,745, of which $79,125 was owed to the city banks of Philadelphia.[2] The facts regarding the mismanagement of the bank were brought out by the report of a committee of Congress in 1819 and caused many demands for the repeal of the charter. Langdon Cheves was elected President, March 6, 1819, and he adopted heroic measures to restore the bank to solvency.

[1] Poor, 486.

[2] Bolles, II., 326.

He borrowed $2,500,000 in specie of the Barings, who were considerable holders of the bank stock, forbade the issue of notes in the South and West when exchanges were against the branches, which was almost invariably the case, and in dealings with the government insisted upon the interval between the transfer of funds and their disbursement which was actually required for the transfers. The bank was saved and was conducted with comparative prudence until the breaking out of the war with President Jackson.

The second Bank of the United States undoubtedly contributed for more than a decade to facilitate the transfer of funds from one part of the country to another and to maintain a uniform circulation equal to coin. The rates of domestic exchange, which were necessarily high because of the imperfect means of communication, were materially reduced by the bank. Its policy greatly benefitted commerce, but invited bitter complaints from the private dealers in exchange, who had been enabled to make excessive profits while the currency was below par because of its different values in different States and the constant fluctuations in these values. The bank, in the language of the report of Senator Smith of Maryland in 1832, furnished "a currency as safe as silver, more convenient, and more valuable than silver, which through the whole Western and Southern and interior parts of the Union, is eagerly sought in exchange for silver; which, in those sections, often bears a premium paid in silver; which is, throughout the Union, equal to silver, in payment to the government, and payments to individuals in business." Mr. McDuffie, who submitted the minority report in the House at the same time, declared that "The whole business of dealing in domestic bills of exchange, so essential to the internal commerce of the country, has been almost entirely brought about within the last eight years. In June, 1819, the bank did not own a single dollar of domestic bills; and in December, 1824, it owned only to the amount of $2,378,980; whereas it now owns to the amount of $23,052,972."[1]

[1] House Rep., 460, 22d Cong., 1st Sess., 312.

One of the most serious charges of evasion of law, brought against the bank in 1832, was in the issue of branch drafts to circulate as currency. Several appeals were made in vain to Congress to modify one of the provisions of the charter requiring the president and principal cashier to sign all the circulating notes. The volume of circulation necessary to do business was so great that the physical labor of signature could not well be performed by those officers. Congress neglected to act and in 1827 an opinion was obtained from Horace Binney, in which Daniel Webster and William Wirt concurred, that there was no legal obstacle to the issue of checks drawn by officers of the branches upon the parent bank, printed for even amounts in similar form to bank-notes. Drafts of this sort for $5 and $10 were authorized by the board of directors on April 6, 1827, and denominations of $20 were issued in 1831. They became a common medium of circulation in the South and West and were accepted in payments to the United States Treasury.[1] The branch drafts outstanding in April, 1832, were $7,410,090. They simply served the purpose of currency without conforming strictly to the intent of the law, in much the same manner as the checks of the London Cheque Bank or the temporary issues in the United States during the panic of 1893.

The Bank of the United States fell because so great an institution in a representative republic could not escape political entanglements and the suspicion of the abuse of political power. President Jackson surprised the financial world by the announcement, in his first annual message in 1829, that "Both the constitutionality and the expediency of the law creating the bank are well questioned by a large portion of our fellow-citizens; and it must be admitted by all, that it has failed in the great end of establishing a uniform and sound currency." The bank was at this time under the presidency of Nicholas Biddle, who succeeded

[1] Letter of Sec. Rush to Nicholas Biddle, Jan. 21, 1820. House Rep., 460, 22d Cong., 1st Sess., 55. The authority to receive these drafts for public dues was revoked by Secretary Woodbury, to take effect January 1, 1835.

Cheves in 1823, and was one of the most imposing institutions of the country. The President's message, therefore, was in the nature of a thunderbolt from a clear sky. Jackson's hostility was due to a complaint by Isaac Hill, a New Hampshire politician who had been made Second Comptroller, that Mr. Mason, the manager of the branch at Portsmouth, New Hampshire, had shown partiality to the political opponents of General Jackson and that his conduct had been "calculated not less to injure the institution than to disgust and disaffect the principal business men." "No measure short of his removal," in Hill's opinion, "would tend to reconcile the people of New Hampshire to the bank."

The truth appears to have been that Mason had excited hostility by his energetic contraction of discounts at Portsmouth and his efforts to correct previous mismanagement. Levi Woodbury, who had defeated Mason for the United States Senate in 1824, addressed a letter early in July, 1829, to Mr. Ingham, the Secretary of the Treasury, making complaints against Mason's management, which Ingham forwarded to President Biddle for his consideration. Biddle was a ready writer, he occupied one of the most powerful positions in the country, he was surrounded by flatterers and sycophants, and he was quickly entrapped into a quarrel which resulted in the overthrow of the bank. He not only denied that the bank had shown political favor at Portsmouth or elsewhere, but went out of his way to declare that the governing board acknowledged no responsibility whatever to the Secretary of the Treasury in regard to the political opinions of the officers of the bank and that it was carefully shielded by its charter from executive control. So fixed had become the relations between the bank and the Treasury in the handling of public monies, and so much a matter of mere routine, that Biddle appeared to overlook the possibility of the withdrawal of the public deposits. He evidently had no realizing sense of the danger which hung over his head or of the spirit of hostility which was being aroused in the mind of Jackson.

The President's suggestions in his annual message excited the fear for a moment that he had information which was not known to the public and bank shares dropped from 125 to 116, only to recover to 130 after a report by a committee of Congress. The portions of the message relating to the bank were referred to committees in both houses, both of which exonerated the bank from the charge of bad management and condemned the suggestion of the President, whether a national bank, "founded upon the credit of the government and its revenues, might not be devised which would avoid all constitutional difficulties, and at the same time, secure all the advantages to the government and country that were expected to result from the present bank." The House on May 10, 1830, tabled, by a vote of 89 to 66, resolutions that the House would not consent to the renewal of the bank charter and on May 29th tabled, by a vote of 95 to 67, resolutions calling for a comprehensive report of the proceedings of the bank.[1] Similar votes in favor of the bank were given in the Senate. The President was mild in his allusions to the subject in the annual messages of 1830 and 1831 and the Secretary of the Treasury was even allowed in the latter year to incorporate in his annual report a strong argument in the bank's favor. It is not improbable that Jackson might have been persuaded by the eminent financiers of his party to consent to a re-charter if the matter had not been made an issue by Henry Clay in the presidential campaign.

The political dangers of a great central bank were demonstrated in the campaign of 1832. President Jackson had given the country in the main a firm and successful administration and it was necessary for Clay and the Whigs to create political issues upon which to make a respectable contest against him. There were dangers in making the tariff the controling issue, because different Whig States were on both sides of the question. Clay determined to make the campaign upon the issues of internal improvement and the recharter of the bank. It was natural that he should

[1] Sumner, *Andrew Jackson*, 247.

accept the sentiment of the financial portion of the community in favor of the bank as the sentiment of the whole and he was so confident of success that he feared Jackson would evade the issue. The resolutions adopted at Baltimore on December 12, 1831, at Clay's instigation, declared that the President, "is fully and three times over pledged to the people to negative any bill that may be passed for rechartering the bank." Biddle and the real friends of the bank who were not politicians protested strongly against making the recharter a party issue, but Clay forced them to the choice between sustaining his party as the friends of the bank or going without political friends. Professor Sumner declares that "Jackson never was more dictatorial and obstinate than Clay was at this juncture." [1]

The fight was opened in the Senate on January 9, 1832, when Senator Dallas presented the memorial of the bank for the renewal of its charter. Biddle came to Washington, opened headquarters, gave sumptuous entertainments, and defended the bank vigorously before the committee of investigation appointed by Congress. The bill for the recharter was passed through both houses, only to encounter a veto message from President Jackson on July 10th. The issue was thus made up for the presidential election, exactly as Clay desired it, but the response of the people was 219 electoral votes for Jackson, 49 for Clay, and 18 for all others. The executive triumphed, as usual in a contest with Congress, and the doom of the bank was decided.

The bank had five years of life before it. Its credit was good and it still held the public deposits. It was not generally supposed that these would be withdrawn until near the date for the termination of the charter, as had been the case with the public deposits in the first Bank of the United States. Jackson's blood was now up, however, and he needed no further stimulus to crush his enemy. The bank made two serious blunders during 1832 and 1833 in its relations with the Treasury. It undertook to make a private arrangement with the Barings regarding the payment of

[1] *Andrew Jackson*, 257.

$5,000,000 of government three per cent. securities, which the Secretary of the Treasury had notified the President of the bank as early as March 24, 1832, would be paid from the surplus revenues. A contract was made through a private agent of the bank for extending these securities, which were to be assumed by the bank and the interest paid to the government. The object was to retain possession of the public money, on deposit with the bank, which was worth seven per cent. in the discount market, rather than permit it to be withdrawn for the redemption of the debt. When the circular of the Barings got into the newspapers in October, Biddle was obliged to disavow the contract and made a lame explanation to Secretary McLane for seeking to delay the payment. The other case was the attempt to collect damages upon the amount of a bill of exchange drawn upon the French government, which was refused payment by the French Minister of Finance, because the money had not been appropriated by the Chambers. The bill was taken up by the Paris agents of the bank, and charged against it. Secretary McLane paid the principal, $961,240, which had been covered into the Treasury, back to the bank and offered to pay actual costs. The bank insisted upon fifteen per cent. damages, under a law of the District of Columbia relating to protested paper, and deducted the amount from the government dividends. The government sued and the Supreme Court decided against the bank.

Performances like these on the part of President Biddle convinced Jackson that the bank was weak and confirmed his purpose to suspend the further deposit of public monies in its custody.[1] Mr. McLane was transferred from the Treasury to the State Department during the spring of 1833 and William J. Duane of Pennsylvania was made Secretary of the Treasury. Duane was a conservative and able lawyer, with little of the politician in his make-up, and when

[1] Jackson also believed that if the bank retained the public funds, it would be able to buy up the votes in Congress necessary to make two-thirds and pass a recharter bill over his veto.—Sumner, *Andrew Jackson*, 299.

the President insisted upon his suspending deposits in the Bank of the United States and making them in future in the State banks, Duane refused to comply and the President removed him from office. Roger B. Taney, who afterwards became so odious in the free States as Chief Justice of the Supreme Court, was transferred from the Department of Justice to the Treasury on September 23d, and began the deposit of the public funds in the State banks.

The contest which followed in Congress belongs to the history of politics rather than that of finance. The Senate rejected the nomination of Taney for Secretary of the Treasury and rejected the President's nominees for government directors of the bank, apparently upon the remarkable ground that they were disposed to insist upon too accurate a knowledge of the bank's affairs. The Senate called for the paper which Jackson had read in the cabinet regarding the removal of the deposits on September 18th, and received the reply that the Senate had no constitutional right to interrogate him on the subject of his communications with his heads of departments. Clay introduced a resolution which was passed on March 28, 1834, by a vote of 26 to 20, declaring that the President had, "assumed upon himself authority and power not conferred by the Constitution and the laws, but in derogation of both." The President sent a protest against this resolution to the Senate on April 17th, which that body ten days later voted, 27 to 16, was a breach of the privileges of the Senate and should not be entered on the journal. The friends of Jackson appealed to the people and gained enough seats in the Senate to pass resolutions on January 16, 1837, expunging the previous resolutions from the records.

The Bank of the United States obtained a charter from the State of Pennsylvania on February 18, 1836, for thirty years. The bank agreed to pay a bonus of $2,000,000 to the State and $100,000 per year for thirty years, besides various subscriptions to the stock of transportation routes, which Benton described as bribery of the legislature and the people. The shares in the bank owned by the United States, amounting to $7,000,000, were paid in four annual instalments at

the rate of 115.58. New stock was sold to replace the government stock, leaving the capital intact at $35,000,000. The capital was too large for local commercial needs and Biddle branched out into loans on stocks of uncertain value, many of which proved worthless after the crisis of 1837. The bank suspended at that time with the other banks of the country, but was compelled to suspend again in 1838, and again in 1841, after which it went into liquidation. The creditors were paid, but the shareholders lost their entire interest. Biddle had resigned in March, 1839, leaving the bank, according to his view, in a prosperous condition. He was indicted during the liquidation for conspiracy to defraud the shareholders. The indictment was quashed, but Biddle was ruined financially and died within five years insolvent and broken-hearted.[1]

The principal items in the accounts of the second Bank of the United States up to the time of its final suspension are shown in the following table :

YEAR.	LOANS.	DEPOSITS.	CIRCULATION.	SPECIE.
1820	$31,401,158	$ 6,568,794	$ 3,598,481	$ 3,392,755
1830	40,663,805	16,045,782	12,924,145	7,608,076
1834	54,911,461	10,838,555	19,208,379	10,039,237
1835	51,808,739	11,756,905	17,339,797	15,708,369
1836	59,232,445	5,061,456	23,075,422	8,417,988
1837	57,393,709	2,332,409	11,447,968	2,638,449
1838	45,256,571	2,616,713	6,768,067	3,770,842
1839	41,618,637	6,779,394	5,982,621	4,153,607
1840	36,839,593	3,338,521	6,695,861	1,469,674

The present method of dealing with public monies in the United States is one of the results of the war over the United States Bank. Secretary Taney, under Jackson's instructions, deposited public money in certain State banks,—most of them selected because their officers were friendly to the administration and characterized by its critics as the "pet banks." The government imposed upon them the conditions of giving security in certain cases, of issuing no small

[1] Sumner, *Andrew Jackson*, 342.

notes and of keeping one-third of their reserve in specie.[1] The State banks undertook by mutual agreement to honor each other's notes and drafts, but the crisis of 1837 caused a general suspension and the payment of $25,000,000 of the deposits in bank-notes bearing an average depreciation of ten per cent. Secretary Taney in his report for 1834 urged legislation to sanction the use of the State banks as depositaries, but the bill prepared on the subject failed in the Senate. The suspension of the banks in 1837 led President Van Buren, in his annual message of that year, to recommend that the public funds be kept exclusively by public officers and that nothing but specie be received for dues to the government. This plan—embodying substantially the features of the present independent treasury system—was several times defeated, but was finally enacted June 30, 1840. One-fourth of all dues to the Treasury were to be paid at once in specie, and an additional fourth each year until the whole were thus paid.

The success of Harrison and the Whigs resulted in the repeal of the independent treasury law August 13, 1841, and two national bank bills were passed, only to be successively vetoed by President Tyler. The public monies were deposited in the banks or not, at the discretion of public officials, until 1846, when the independent treasury system was again established by authority of Congress. The policy of refusing State bank-notes for government dues continued until the creation of the national banking system during the Civil War. That system gave the government the security of its own bonds for the bank-notes, and the national banking act provided that the notes should be "received at par in all parts of the United States in payment of taxes, excises, public lands, and all other dues to the United States, except for duties on imports; and also for all salaries and other debts and demands owing by the United States to individuals, corporations, and associations within the United States, except interest on the public debt, and in redemption

[1] Kinley, 17.

of the national currency."[1] The national banks were again made the depositaries of public money during the first administration of President Cleveland, but were required by the Secretary of the Treasury to deposit United States bonds as security for such monies in much the same manner as for the security of national bank-notes. The amount of deposits in the banks on August 1, 1888, when Secretary Fairchild made a report on the subject to Congress, was $54,475,055, exclusive of $4,052,021 on deposit to the credit of disbursing officers. The number of banks among which these deposits were distributed was about three hundred and the largest deposit was $1,100,000. The policy of Secretary Windom and the absorption of the surplus reduced these deposits after 1892 and their entire amount on January 2, 1896, was $14,271,280. The independent Treasury continues to transact the bulk of the public business and sub-treasuries are maintained at New York, Philadelphia, Boston, Baltimore, Cincinnati, Chicago, St. Louis, New Orleans, and San Francisco.

[1] Act of June 3, 1864, Sec. 23.

CHAPTER XIV.

THE STATE BANKING SYSTEMS.

The Condition of the Country When They were Adopted—Success of the Suffolk System and of Banking on General Assets—The New York Safety Fund and Security Systems—Unhappy Experience in the West and South with Banks of State—The Effects of the Civil War—Failure of the Security System—General Statistics of the State Banks.

THE systems of banking authorized under the laws of the various States of the United States offer examples of nearly every form of note issues and every degree of success or failure. The economic development of the country between the Revolution and the Civil War was in an experimental stage as well as its political development. The rules of sound banking had not yet been worked out even in the older countries of Europe, as the mistakes and failures of English, French, and Austrian banking abundantly show; but to ordinary sources of error and risk were added in the United States the elements of experiment and uncertainty in every department of human activity. The Englishman or Frenchman might not be a good banker, but he could at least form an intelligent estimate of the volume of trade with which he had to reckon and the conditions under which it was carried on. His problem was simply to work out, according to sound rules, a mathematical problem for which the necessary elements were known. With the American, on the other hand, every element was an unknown quantity. He had to guess at the first element in his equation, and if he guessed wrongly absolute accuracy in

his further computations could not possibly yield a true result.

A new country, poor in specie and in loanable capital, is almost forced by the necessities of her situation to adopt monetary devices which would not be tolerated under better conditions. Some of these devices would be comparatively harmless if their true character were understood and they were used with moderation ; but their tendency is misleading and intoxicating to the average mind and they are usually so abused as to offset the little benefit which might be derived from them. The most successful banking systems under State law in the United States were those of New York and New England, where the surplus capital of the country in the earlier days was concentrated. The least successful systems were in the newer and poorer sections of the country and they grew progressively worse as inexperience and poverty seemed to make more imperative the necessity for creating something out of nothing. Four distinctly marked systems of note issue were in operation in the United States side by side almost up to the close of the Civil War and it is not surprising that the conglomerate currency which they created has left unsavory memories behind it. These four systems were : Issues upon general assets ; issues protected by a general safety fund ; issues based upon public securities ; and issues based upon the faith and credit of the States.[1]

[1] The principal sources for the preparation of this chapter have been the monographs prepared by Mr. L. Carroll Root for the "Sound Currency Committee" of the New York Reform Club ; the report of John J. Knox, the United States Comptroller of the Currency, for 1876 ; the report prepared by Mr. Henry H. Smith, Assistant Register of the Treasury, in response to Senate resolutions of July 26, 1892, printed as Sen. Ex. Doc. 38, 52d Cong., 2d Sess. ; and the report of Comptroller A. B. Hepburn for 1892. The investigations of these gentlemen have brought together and co-ordinated a mass of material which would otherwise have to be sought with great labor from a variety of sources. Mr. Root has further favored me with an examination of this chapter and the suggestion of some changes, which I have adopted.

The best illustration of the system of banking upon general assets is afforded by the banks of New England, and especially by the banks of Boston, which became the centre of the New England redemption system. The note issues of the New England banks were permitted in many cases to exceed the proportion to capital which is now considered safe, and they were not subject until late in their history to thorough official supervision; but in spite of these defects of the system, the notes usually circulated at par and specie was attracted to New England when driven from other sections of the country by depreciated paper. The first local bank in New England, and the second of the kind in the United States, was incorporated by act of the General Court of Massachusetts on February 7, 1784, with a maximum capital of $300,000, and was called the Massachusetts Bank. No limitations were imposed in the original Massachusetts law upon note issues, but an act of 1792 prohibited notes below $5, and the bank was directed to limit the amount of notes, together with "money loaned by them by a credit on their books or otherwise," to "twice the amount of their capital stock in gold and silver, actually deposited in the banks and held to answer the demands against the same." A general law was passed in 1799, prohibiting banking by unincorporated companies or the further issue, except by the Nantucket Bank, of notes below $5. This provision was modified in 1805 so as to permit the issue of bills of $1, $2, and $3 to the amount of five per cent. of paid-up capital. This limit was increased in 1809 to fifteen per cent., reduced in 1812 to ten per cent., and again increased in 1818 to twenty-five per cent., which remained the limit during the life of the State banking system.[1]

An act was passed in 1803, requiring semi-annual reports of condition by the Massachusetts banks to the State officials, and it appeared that at that time seven banks were in operation with a capital of $2,225,000 and a circulation of $1,565,000. An attempt was made in 1811 to found a State

[1] Root, *New England Bank Currency*, "Sound Currency," Vol. II., No. 13, p. 4.

bank occupying a similar relation to the Commonwealth that the United States Bank had occupied towards the national government, but the State capital was never subscribed and the authorized capital was reduced in 1817 from $3,000,000 to $1,800,000.[1] The charter of this bank and of the Merchants' Bank, also incorporated in 1811, served as the model from which most subsequent charters in Massachusetts were drawn. One-fifth of the capital was required to be actually paid in before the beginning of business; the stockholders were individually liable to the amount of their stock in case of loss arising from mismanagement, and the liabilities, exclusive of deposits, were limited to twice the amount of the capital. The limit upon circulation, which was thus incidentally imposed, was reduced in the case of most of the later banks to 150 per cent.

The Massachusetts and other New England banks maintained specie payments in 1814, when those of other parts of the country suspended, and the current of specie towards New England swelled the holdings of the Massachusetts banks alone, from $1,513,000 in 1811 to $6,946,542 in 1814. The total banking capital authorized had increased in 1828 to $9,075,000 and thirty-six new banks were incorporated in the four years ending with that date. A new banking law was passed on February 28, 1829, which applied to banks thereafter incorporated and to those obtaining an increase of capital or an extension of their charters. The limit of the notes which a bank might circulate was reduced to 125 per cent. of the capital and the total of the debts, exclusive of deposits, was limited to twice the capital. A provision was made against the practice of issuing notes promising pay-

[1] The State subscribed $400,000 to the capital of the Union Bank of Boston, which was incorporated in 1792, and was generally a subscriber at the formation of new banks for the next twenty years. About $1,000,000 of bank stock in this way came into the hands of the State and afforded a generous dividend until it was sold in 1812 to meet some unusual expenses. The State does not seem to have abused its share in the ownership by interference with the management of the banks.—Martin's *Boston Stock Market*, cited in Comptroller's Report for 1876.

ment with interest at a future date, by which the banks had endeavored to escape the obligation to pay cash on demand to depositors and note-holders. An effort was made to evade this provision by issuing deposit books, making the same promise. They were first issued mainly to depositors, but they came to be extensively issued during the pressure of 1834 in discounting paper. The General Court passed a law in that year prohibiting the practice.

The organization of banks in Massachusetts proceeded with alarming rapidity during this period of speculation, and at the end of 1836, seventy-eight new banks had been added to the sixty-two older banks, and forty-three of the latter had obtained an increase of capital. Several banks succumbed towards the close of the year, but the Boston banks were mainly sound and followed the New York banks reluctantly on May 12, 1837, in the suspension of specie payments. An act of 1809 imposed a penalty of two per cent. a month on banks which failed to redeem their notes in specie. This provision was not enforced in 1837, and the General Court suspended it until January 1, 1839, in the case of banks which kept their circulation within seventy-five per cent. of their capital, redeemed notes below $5 in Boston, and below $3 elsewhere, and complied with some other conditions. Voluntary resumption took place throughout the State on August 13, 1838. Failures still continued among the mushroom institutions which had been created during the period of speculation, and thirty-two Massachusetts banks wound up their affairs between 1837 and 1844. The necessity of more efficient supervision by the State was made plain by the crisis of 1837, and three bank commissioners were authorized to make annual examinations of all the banks and special examinations when they thought proper. This law was repealed after five years, but the Massachusetts banks were now upon a sound basis and failures were few during the twenty-five years before the creation of the national system. Only two failures occurred between 1840 and 1855, and the notes in both cases were paid in full.

Most of the bank charters were renewed for twenty years

in 1831 and expired on October 1, 1851. The renewal in the latter year was made the occasion of several changes in the banking laws. One of these revived the board of bank commissioners with the same powers of examination as in 1838. Another change of law imposed liability upon stockholders for the redemption of notes, in case of failure, to the amount of their stock, without the former limitation in regard to mismanagement. The speculative mania which preceded the crisis of 1857 resulted in the creation of fifty-eight new banks in Massachusetts with a capital of $14,400,000 and 157 increases in the capital of existing banks, amounting to $18,745,000. Several failures took place, but the noteholders suffered little loss and a committee of the legislature in 1856 reported against the granting of further charters. The condition of the State banks of Massachusetts in 1862, just before absorption into the national system, showed 183 banks in operation with a capital stock of $67,544,200; circulation, $28,957,630; deposits, $44,737,490; loans and discounts, $127,592,511; and specie, $9,595,530.

The banking systems of the other New England States were generally based upon the principle of issuing notes against assets and the banks maintained close relations with those of Boston. The legislature of Maine took advantage of the expiration of a number of charters in 1846 to adopt some changes of law to afford greater security for circulating notes. The Act of August 10, 1846, provided that for the amount of circulation issued in excess of fifty per cent. of the capital, one dollar in specie should be kept for three dollars in bank-notes and that the total circulation should never exceed the capital plus the amount of specie on hand. The State of Vermont created in 1831 a safety fund modelled closely upon that of New York. Each bank thereafter chartered was required to pay into the State Treasury, in six annual instalments, the sum of four and a half per cent. upon the amount of its capital stock, and in case the fund was reduced by the failure of any bank it was to be restored by assessments by the State Treasurer, not exceeding three-fourths of one per cent. in any one year upon the capital of

the banks. An act was passed by the General Assembly in 1842, relieving the banks from contributions to the safety fund in case the directors should execute satisfactory bonds to redeem according to law all bills issued and to pay deposits on demand.

The banking laws of Rhode Island were peculiar in the facilities which they extended to banks for recovering debts. The first bank charter,—issued to the Providence Bank in 1791, and creating the fifth chartered bank then existing in the United States,—provided that upon any note or other instrument expressly made payable at the bank, the President or certain of the directors might cause a demand to be made upon the debtor, in case of his failure to make payment at maturity, and in case the obligation remained unpaid for ten days, these officers might write to either of the clerks of the courts of common pleas or of the superior court and order such clerk to issue a writ of execution *capias satisfaciendum fieri facias*, and attachment of real estate upon which the debt and costs might be levied, whereupon the clerk was required to issue such an execution, to be served by any sheriff or deputy. Subsequent charters did not even require demand in writing or protest, but authorized the officers of the bank to order the clerk of one of the courts to proceed to issue the execution. This drastic method of collecting debts under the "bank process" made banks very popular investments with capitalists and accounted for their rapid increase up to 1818. An act was passed forbidding the further granting of such charters, but the decision of "the Dartmouth College" case in the Federal courts, denying the power of the grantor of a charter to change the terms except with the consent of the grantee, delayed any provision for withdrawing the powers of the "bank process" from banks already possessing them. The arbitrary character of this process and the hardships it inflicted aroused strong popular feeling and resulted in an act of 1836 abolishing the privileges of "the bank process" and limiting the banks thereafter to the same remedies as individuals for the collection of debts. Sixty-one

banks then existed in Rhode Island, of which thirty possessed the powers of the "bank process."

The peculiar feature of the New England bank circulation was the Suffolk system of redemption, which was established in order to protect sound banking currency from being driven out of circulation by the inferior currency of other States. The suspension of specie payments south and west of New England in 1814 resulted in the introduction of depreciated notes across the Connecticut border and drove the Connecticut bank-notes into private hoards or brought them to the banks for redemption in specie.[1] The banks of Maine encountered a similar situation prior to the suspension of specie payments in 1837. They were forbidden by law to issue notes below $5, with the object of keeping the currency saturated with coin, but this purpose was defeated by the circulation of the small notes of the banks of neighboring States. The banks of Boston found themselves, even before the close of the last century, under somewhat the same competition from the country banks of Massachusetts. The Boston banks at first undertook to send the country notes promptly home for redemption, but the banks protested against this policy. The Boston banks then refused to receive the country notes altogether. The result was the hoarding of "Boston money," which was sold at a small premium to persons having payments to make at the banks, while the channels of circulation were filled with the country notes, which were known as "foreign" or "current money."

Several attempts were made in Boston to establish a redemption office for sending notes home for redemption, but it was not until 1813 that a systematic method of clearing and redemption for bank-notes was put in operation by the New England Bank. The discount on the notes of "foreign" banks was larger than the actual expense of redemption justified, and the New England Bank gave notice that it would charge only the actual cost of sending foreign money home for redemption and obtaining the specie for it. The execution of their plan brought down

the discount on "foreign" notes from four or five per cent. to one per cent. for notes of Massachusetts banks and somewhat more for those of other States.

The Suffolk Bank was incorporated in Boston in 1818 and the directors determined to give special attention to foreign exchanges. A committee appointed to consider the subject in 1819 reported that it was expedient "to receive at the Suffolk Bank the several kinds of foreign money which are now received at the New England Bank, and at the same rates." They recommended that if any bank should make a permanent deposit of $5000 with the Suffolk Bank, with such further sums as were necessary from time to time to redeem its bills taken by the Suffolk Bank, such bank should have the privilege of receiving its bills at the same discount at which they were purchased. They recommended that the banks of Providence and Newport and twenty-three others keeping an account with the Suffolk have the privilege of receiving such of their bills as were received by the Suffolk bank at the same discount as taken, without the permanent deposit of $5000, provided these banks would make all their deposits at the Suffolk Bank and at all times have money to redeem the bills taken.[1] The policy to be adopted towards banks refusing to make a deposit was to send their notes home for redemption. These recommendations were put in force and the lively competition of the Suffolk with the New England Bank soon forced exchange on Massachusetts notes to one-half of one per cent., or even less.

The notes of the Boston banks were still crowded out of circulation by the slight discount on the notes of the country banks and it was found in 1824 that the permanent circulation of the eleven city banks, with a capital of $11,150,000, was not more than $300,000, while the country banks, with a capital of less than $9,000,000, had a circulation of $7,500,000. An agreement was made between the Suffolk and six other Boston banks by which a fund of $300,000 in their notes was furnished the Suffolk, to be paid out in

[1] Whitney, 7–8.

equal proportions in the purchase of country bank-notes.[1] The tendency of this policy was to force the city notes into circulation and withdraw the country notes unless they were maintained absolutely at par by the action of the country banks. The plan was vigorously resisted at first by the country banks and the Boston association was decorated with such opprobrious names as the "Holy Alliance" and "Six-tailed Bashaw." The country banks were forced to yield, however, and most of them consented to make the permanent deposit of $2000 which was now required, in addition to a sufficient sum for current redemptions. The notes of those maintaining their redemption fund were received at par and were charged up against them once a week or as often as might be convenient. The Suffolk Bank charged interest whenever the amount redeemed exceeded the funds to the credit of the issuing bank, but received the notes of all banks in good standing and placed them to the credit of the bank sending them in.

A sort of clearing house was thus established which enabled the issues of one bank to be set off against those of another in making settlements. The effect of restoring the country notes to par was to reduce the circulation of sixteen Massachusetts banks within six months by $382,781 and to increase the circulation of the Boston banks by $283,497. When any bank refused to join the Suffolk system, the Suffolk Bank simply presented its notes for redemption. This course soon convinced the majority of the country banks that it was better to clear through the Suffolk Bank than to maintain an unequal competition with neighboring banks, which had the prestige of belonging to the Suffolk system and whose notes were at par throughout New England. The suspension of specie payments in 1837 put an end to enforced redemption for a time, but the majority of the banks continued to settle their balances through the Suffolk Bank and their bills passed current all over the

[1] John Amory Lowell, who served on the "Foreign Money Committee" for forty-two years, and William Lawrence, prepared this plan and report.

Union, while those of the other banks had only a local circulation.[1]

A branch redemption agency was established in Rhode Island, by which the Merchants' Bank of Providence received at par from the Rhode Island banks the bills of all other banks in New England and settled balances as far as possible among the Rhode Island banks. Bills issued by banks outside of Rhode Island were sent to Boston, and Rhode Island bills were sent in bulk by the Suffolk Bank to Providence. Legal encouragement was given to the Suffolk system in Vermont by the Act of 1842, which levied a tax of one per cent. upon bank capital, but remitted the tax to any bank which should "keep a sufficient deposit of funds in the City of Boston, and should at that city uniformly cause its bills to be redeemed at par." All but three of the Vermont banks were members of the system before 1848 and in 1850 all had joined. Several of the Maine banks resisted for a time and received the support of the bank commissioners in 1837, but their circulation became limited to their immediate locality and the system was commended by the commissioners in later reports.

The handsome profits derived by the Suffolk Bank from the redemption system led to several efforts to establish a rival institution. The work of the Suffolk Bank was so well done that it was not until 1855 that these efforts bore tangible fruit. The Bank of Mutual Redemption was then established for the specific purpose of redeeming the currency of the New England banks at par. The bank went into operation in 1858, with 135 New England banks interested as stockholders and thirty-five keeping a permanent deposit aggregating $143,000. The bank was admitted to the clearing house after a struggle and most of the country

[1] "At the time when the Suffolk system was at its best I lived in Chicago. The notes of Massachusetts banks were in great request there. They were considered the best currency going and they bore a premium over the notes of Illinois and Wisconsin banks." Testimony of Horace White before House Committee on Banking, House Report 1508, 53d Cong., 3d Sess., 84.

banks withdrew from the Suffolk and transferred their deposits to the Bank of Mutual Redemption. There was some friction between the two institutions and it was feared in some quarters that the entire system would be endangered, but a mutual exchange of the notes of their patrons was arranged between the two banks. The Suffolk Bank withdrew from the system on November 1, 1858, upon the ground that "its main feature, the right to send home bills for specie, cannot be given up without destroying its efficacy," and that "under the existing circumstances the bank does not wish to stand in the way of a trial of the attempted experiment of a foreign money system to be conducted on less stringent principles." The Suffolk Bank continued to receive country money at a discount of twenty-five cents per $1000 and to share to this degree in the business of redemption.

The circulation of the New England banks in 1858 was less than $40,000,000 and the redemptions for that year through the Suffolk Bank were $400,000,000. Every note, therefore, on the average, passed through the redemption agency ten times a year, or a little less often than once a month. This frequency of redemptions not only tested the solvency of the banks by the ultimate test of a banking currency, but it kept the circulation constantly adjusted to business conditions. The redemptions through the Suffolk agency were $76,248,000 in 1834 and increased to $105,457,000 in 1837. There were fluctuations during the period of specie suspension, but the redemptions increased progressively to $137,000,000 in 1845, $220,000,000 in 1850 and $341,000,000 in 1855, until they reached their maximum of $400,000,000 in 1858. The expenses of carrying on the redemption agency reached a maximum of $40,000 in 1858, making an average expense of ten cents per $1000. The suspension of specie payments by the banks of the country at the close of 1861, as the result of Secretary Chase's issue of government demand notes, arrested the regularity of redemptions through the Suffolk system and it was superseded before resumption by the National banking system. The Suffolk system was never

sustained by formal law, but it maintained New England bank currency for a generation at par with gold and prevented any losses to note-holders larger than a fraction of one per cent. of the entire volume of circulation.

New York tried two banking systems under which many strong banks were created, but both of which failed in some degree through defects of detail. The early New York banks issued notes against their general assets and were chartered under special acts of the legislature, which were granted to some extent as political favors. The Bank of New York was incorporated by Act of March 21, 1791, after having done business for seven years under articles of association drawn by Alexander Hamilton. This bank retained a practical monopoly in New York City until 1799, when the Manhattan Company began a banking business with a capital of $2,000,000. The charter was obtained by the management of Aaron Burr and would undoubtedly have been refused by the Federalist majority in the legislature if it had been clearly understood that it carried banking powers; but the charter was granted for the avowed purpose of supplying the City of New York with pure water and cloaked the banking power under a general provision permitting the company to employ its surplus in any moneyed transactions not inconsistent with the laws of the State.[1] Six additional banks were chartered up to 1811; nine additional in that and the following year, after the lapse of the charter of the Bank of the United States; and twenty-four more from 1813 to 1825.

Thirty New York bank charters were to expire between 1829 and 1833, and Governor Van Buren in the former year urged upon the legislature a sweeping measure of reform. He presented what is known as "the safety-fund plan," which he stated had been presented to him by Mr. Joshua Forman of Syracuse. Mr. Forman declared that "The propriety of making the banks liable for each other was suggested by the regulations of the Hong merchants in Canton, where a number of men, each acting separately,

[1] Roberts, 477.

have, by a grant of the government, the exclusive right of trading with foreigners and are all made liable for the debts of each in case of failure." Mr. Forman did not propose to extend this principle further than the guarantee of the circulating notes, but by accident or design the bill which passed the legislature made the safety fund liable for all the debts of a failed bank. Each bank was required to pay annually to the Treasurer of the State a sum equal to one-half of one per cent. of its capital stock until the payments should amount to three per cent. The first act, approved April 2, 1829, provided for the distribution of the assets of a failed bank in the usual way and that, after all the assets had been turned into money and the final distribution made, a court of chancery should enter an order showing the amount necessary to discharge the remaining debts and should authorize the Comptroller to pay the amount from the bank fund. This law was modified by the Act of May 8, 1837, to enable the State authorities to take such measures as might be necessary for the immediate payment of the notes of any insolvent bank whose liabilities in excess of assets should not exceed two-thirds of the bank fund. It was not until 1842, after the failure of nine of the banks incorporated under the safety fund system, that an act was passed making the circulating notes only a charge against the safety fund and leaving the other liabilities of the failed bank to be paid from the assets.

The panic of 1837 put the safety fund to its first test and compelled the State Comptroller to make heavy payments in the redemption of circulating notes. Three important banks in Buffalo failed early in May, 1837, with a reported circulation of $413,961. The Comptroller announced that their bills would be received in payment of canal tolls and other debts to the State and they were maintained substantially at par. The charters of two banks were repealed by the Legislature in 1837 and their notes redeemed by the State, but one of these charters was renewed and the payments from the safety fund were reimbursed. The safety fund was practically intact in 1840 and stood at $870,615.

The next three years witnessed eleven failures, which practically wiped out the safety fund and compelled calls upon the solvent banks to make it good. The redemption of notes was suspended after the first four failures, because the fund was deemed no more than sufficient to cover their liabilities, but the Act of 1842 permitted the banks to anticipate their annual contributions by as much as six years in some cases and to pay into the fund at par the notes of the failed banks. The banks very generally took advantage of this provision and made a good profit on notes of the failed banks which had fallen into their hands at a considerable discount. Their advance payments did not involve a loss of interest, as the original law required the investment of the bank fund and the payment of interest to the banks, and the Act of 1842 granted seven per cent. interest on the advance payments. Redemptions of notes up to September 30, 1850, were $1,614,577 and payments to other creditors up to 1851 were $1,088,109.

The failure of the Lewis County Bank in November, 1854, with deposits of only $1,998 and outstanding notes for $148,-545, found the safety fund no longer adequate to redeem circulation. Future contributions up to 1860 were pledged for the redemption of the public stocks which had been issued to obtain ready money to provide for previous failures. The notes of the Lewis County Bank were finally redeemed twelve years later and the notes of the three banks which failed in 1857 were provided for out of their assets. The total contributions to the safety fund from its creation to the abolition of the system were $3,104,999.

The safety fund system broke down primarily because the fund was made to cover all liabilities instead of simply the liability for note issues. The fact that another system was adopted for banks organized after 1838 also operated to the injury of the safety fund system, because no new banks became contributors and the failure and withdrawal of some of the old ones gradually reduced the number over whose resources the liability was distributed. Another evil by no means inherent in the safety fund system, but which

increased the demand upon it, was the issue of notes by several of the safety fund banks in excess of the maximum allowed by law. This defect was remedied in 1843 by an act providing for the issue of notes registered and countersigned by the Comptroller and the surrender of the plates with which the banks were then printing their notes. A mistake was made also in basing the contributions of the banks to the safety fund upon their capital rather than upon their outstanding circulation. But the arrest of the expansion of the system, the over-issue of notes in violation of law, and the distribution of the assessment in proportion to capital, would not have prevented the success of the safety fund system if the fund had been maintained exclusively for the redemption of circulating notes. The fund would have amply secured the notes of the New York banks and ensured their prompt redemption at par, even without the reduplicated security afforded by the constitution of 1846, which made the notes a first lien on the assets and made stockholders liable, to the amount of their stock, for the debts of a failed bank contracted after January 1, 1850. A careful estimate shows that the annual assessment required on the average from 1829 to 1865 to keep the fund good and redeem every dollar of the circulation of suspended banks would have been less than one-fourth of one per cent. of the banking capital, or about three-eights of one per cent. on the average outstanding circulation.[1]

Bank charters continued to be granted in New York by special acts and to be subject to political favor after the adoption of the safety fund plan and up to 1838. A campaign for free banking,—in the sense of equal right to all persons complying with fixed conditions,—was waged by

[1] Root, *New York Bank Currency*, "Sound Currency," Vol. II., No. 5, p. 15. Millard Fillmore, who was Comptroller of the State in 1848, showed that up to that time, covering the period of the most numerous failures, the contributions to the safety fund had been $1,876,063 and the outstanding circulation of the failed banks $1,548,558, leaving a surplus of $327,505, if the fund had been used simply to guarantee circulation.

the Loco-Foco Democrats for several years and bore fruit in the Free Banking Act of April 18, 1838. Individuals or associations were authorized by this act to engage in the issue of notes, which were to be delivered to them by the State Comptroller, upon depositing with him the stocks of the United States, of the State of New York, or of any other State approved by the Comptroller, made equal to a five per cent. New York stock. Provision was also made for issuing notes on bonds and mortgages on improved, productive and unincumbered real estate worth double the amount secured by the mortgage, and the notes were to show whether they were secured by stocks or by mortgages. The mortgage feature of the law opened the door to a paper money Saturnalia as dangerous as the issues of Law's Bank, the *assignats* of the National Assembly, or the Land Bank of Norway; but fortunately the conditions attached to the issue of notes for mortgages were somewhat severe and such issues never attained any considerable proportion of the aggregate circulation of the free banks. The provision for mortgages as a basis for circulation was repealed in 1863 and securities for note issues were restricted solely to stocks of the State of New York and of the United States.

Individuals as well as associations were prompt to take advantages of the free banking law and the amount of capital subscribed by January 1, 1839, was $10,838,175. The actual circulation under the law at that time was only $396,300, but the circulation had increased by December 1, 1839, to about $6,000,000, issued by seventy-six persons or associations, with fifty-seven additional applications pending. Eight of these banks went out of business before January 1, 1841, and eighteen more followed in the course of the next year. The notes were redeemed at an average discount of twenty per cent. for those secured by stocks and twenty-five per cent. for those secured by stock and real estate. The results of the sales of securities up to the close of 1850 showed aggregate receipts of $1,142,758 upon stocks which had been accepted as security for circulation to the amount of $1,468,245. This afforded a dividend

of about 77 per cent. upon the circulation thus redeemed. The New York stocks sold on the average for 92.86 per cent.; Michigan stocks came next at 72.95 per cent.; Indiana bringing up the rear at 49.08 per cent.

The fact that individuals could issue notes under the free banking law upon the deposit of securities led to many visionary efforts to exploit credit and resulted in 1844 in legislation requiring an individual banker to deposit securities to the amount of not less than $50,000 and to transact business in the place in which he resided. A market was created in New York for a time for securities which did not find a ready sale elsewhere and quotations for such securities were strengthened, but this market was destroyed by the Act of 1846, limiting the securities thereafter accepted to those of New York. Such changes gradually strengthened the system until there was little to be desired on the single ground of security. The failures during the first twelve years of the free banking system showed losses of $326,000, or only $27,200 per year on an average circulation of about $6,000,000. This was less than one-half of one per cent. per year and the losses in the remaining fifteen years of the operation of the system averaged only $4800 per year on a circulation of about $22,000,000, or less than one-fortieth of one per cent. The circulation issued under the free banking law was not a strong reliance, however, in times of pressure and was threatened at such times, when strength was most needed, by the decline in securities. It had little elasticity and did not meet the demands of the business community in this respect nearly so well as the circulation of the safety fund banks. Defects of detail were gradually eliminated, however, and the system was successful enough to attract attention in Canada in 1850 and to become the model of the national banking system of the United States in 1863.

The banking laws of New York were followed also in many Western States, but not always closely enough to assure the later systems the solidity of the original. The State Bank of Ohio, created in 1845, was one of the best of these institutions and its note issues were protected by a

combination of the safety fund and security principles. The bank was not, as its name might imply, an institution of State, but was owned entirely by individuals and acted as a sort of board of control for the branch banks. Each branch was required to deposit with the board of control ten per cent. of the amount of its circulating notes, either in specie or in the bonds of the State or the United States, as a safety fund for the protection of the entire note issues of the bank. Each branch was liable for the circulation, but not for the other liabilities, of the other branches. The reimbursement of the safety fund for notes redeemed was constituted the first lien on the assets of a failed branch. The State Bank of Ohio was eminently successful and was managed in much the same way as the State Bank of Indiana. The aggregate capital of the thirty-six branches in 1863 was $4,054,700; circulation, $7,246,513; loans and discounts, $8,653,459; deposits, $5,631,629; and specie, $2,216,982.

The State of Michigan enacted a safety-fund law in 1836, but it was forgotten and ignored in the phrensy of paper inflation which swept over the State during the next few years. The first session of the State legislature in 1837 passed a general banking law, which was followed up after the panic in the same year by an act permitting new banks to begin business in a condition of suspension of specie payments. Thirty per cent. of the capital was required to be paid in specie, but this provision was evaded by borrowing specie for a few days when the bank commissioners made their tours of inspection. Any twelve free-holders could form a bank if they were able to show a capital of $50,000, including thirty per cent. in specie and the remainder in bonds and mortgages approved by the Auditor General of the State.[1] The restraints of the law were so recklessly violated that the State was soon flooded with $1,000,000 in worthless bills. Banks were created after specie resumption in the most inaccessible places, that their notes might not be presented for redemption; and Eastern speculators took out

[1] Pelch, Senate Ex. Doc. 38, 52d Cong., 2d Sess., 76.

Michigan charters and issued the bills in other States where the standing of the banks could not be known. "They were at a great discount," says Judge Cooley, "as compared with Eastern bills; the issues of one bank were at a discount as compared with those of another; merchants kept couriers by whom they hurried off to the banks of issue the bills they were compelled to take, that they might if possible exchange them for something in which they had more confidence. No 'circulating medium' ever before circulated so rapidly."[1] Fraudulent over-issues were frequent and in many cases were not even recorded. Misery and bankruptcy spread over the State, with their natural sequence of stay laws and laws fixing the value at which the property of debtors should be taken. The free banks were nearly all in the hands of receivers when, in 1844, the Supreme Court of the State decided that even the receiverships had no legal existence, for the general banking act had been passed in violation of the constitutional provision regarding corporations, which implied the necessity of a separate charter in each case.

Banking laws basing the issue of notes upon securities were adopted by Illinois in 1851, Indiana in 1852, Wisconsin in 1853, and other States soon after. The restrictions which experience in New York showed to be necessary to protect note-holders received little attention in the West and the rapid depreciation of the "red dog" and "wildcat" currency cast a suspicion upon State bank issues which has survived to this day. Fifty-one of the ninety-four free banks of Indiana suspended before the panic of 1857 and most of those left tumbled like a house of cards in all the States when the pressure came. A fictitious market was created for securities, which brought prices that could not have been otherwise obtained, and the stimulus was thus given for the creation of public debt by the issue of securities, the issue of bank-notes on the securities, the purchase of more securities to be used as the pledge of new bank-notes,

[1] *Michigan*, 272.

and so on in an endless chain of debt creation and the inflation of paper wealth. It was usually found when a bank failed that the securities could not be marketed for their face value and in many cases that there were no other available assets. The Bank Comptroller of Wisconsin reported as late as 1863 a list of fifteen failed banks whose notes he was redeeming at rates ranging from sixty cents to ninety-five and a half cents on the dollar.[1] The basis of redemption, however, was not coin, but United States Treasury notes, themselves depreciated about thirty per cent., so that it was necessary to multiply the one depreciation into the other to obtain the scanty proceeds in coin of Wisconsin notes based upon "securities." Free banking laws were passed in eastern States, but the system made little headway in those States against the established credit of the chartered banks.

One of the most dismal chapters in American banking history is that which records the creation and collapse of banks owned and managed by the States. The Federal Constitution sought to close the door against issues of the legal tender paper money, which had worked such havoc with prices and credit during the Revolutionary era, by the decree that no State should "emit bills of credit." The Supreme Court sustained the force of this prohibition in the case of Craig *vs.* the State of Missouri (4 Peters, 410), and decided that the certificates issued by the State and made receivable for salaries and taxes, even though not full legal tender, fell under the ban of the constitutional restriction. A different spirit ruled the court when the case of Brisco *vs.* the Bank of the Commonwealth of Kentucky was decided in 1837. Chief-Justice Marshall had just died, but Justice Story, who dissented from the majority decision, insisted that his dead associate had agreed with him, that the pending case could not be distinguished in principle from that of Craig *vs.* Missouri. The majority found a distinction in the fact that the bills in question were issued by a bank under

[1] *Report of the Secretary of the Treasury on Condition of the Banks at the Commencement of 1863*, 204.

the direction of a president and twelve directors. They held, notwithstanding the fact that the bank was exclusively the property of the State, that the notes were not "bills of credit" within their definition, which included only "paper issued by the authority of a State on the faith of the State, and designed to circulate as money." [1]

The mania for banks of State was already well on its course before this decision was made. The Commonwealth of Kentucky had been part owner in the Bank of Kentucky, incorporated in 1806, and owned $586,400 of the capital stock of $2,726,100 when the charter was repealed in 1822. The Bank of Kentucky was hampered throughout its career by State interference, but was paying specie and its stock was at par when the State decided to set up a rival under its own exclusive ownership and management. The new-comer was the Bank of the Commonwealth of Kentucky, chartered for twenty years by the Act of November 29, 1820, with a capital of $2,000,000, which was increased December 22, 1820, to $3,000,000. The State availed itself of the power to appoint additional directors in the old bank to pack the board with pliant tools, who soon effected its ruin for the benefit of the new institution. The Bank of the Commonwealth, however, was a pitiable failure. Its notes had fallen on March 22, 1822, to sixty-two and a half cents on the dollar and they continued to fall until the entire State was embroiled in a legal controversy which almost ended in

[1] Brisco *vs.* Bank of Kentucky is reported in 11 Peters, 257. Prof. Sumner declares that by this decision "wildcat banking was granted standing ground under the Constitution" and that "the decisions of the Supreme Court on the constitutionality of the Legal Tender Act must have borne an entirely different color, if Marshall's opinion had prevailed in Brisco's case."—*Andrew Jackson*, 363. Judge Story went so far, in his Commentaries on the Constitution, as to intimate that if the question were a new one, it would be doubtful if the States had power under the Constitution to incorporate banks of issue; but it is obvious that the permission to issue notes, circulating, like other commercial paper, upon private credit, is very different from the issue under public authority of legal tender money.—Kent, *Commentaries*, I., 408.

revolution. The hard times of 1818 had resulted in the charter of forty-six banks with a total capital of $8,720,000, but the demand for specie by the United States Bank drove them to the wall and the State was left without solvent banks. A more permanent legacy of the hard times was a replevin law, passed in 1820, which gave debtors two years within which to redeem their goods unless payment was accepted by creditors in notes of the Bank of the Commonwealth.

"The relief laws," of which the replevin law was one, became the political issue of the hour. Judge Clarke, of the Clarke County District Court, declared one of the provisions of the replevin law unconstitutional, as impairing the obligation of existing contracts. The Appellate Court sustained Judge Clarke, in spite of an effort to remove him by an extra session of the legislature, but the relief party swept the State in the elections of 1824, repealed all laws concerning the Appellate Court and created a new Court of Appeals. The Justices of the old court took the ground that their offices were created by the Constitution and could be abolished only by constitutional amendment. Their records were taken from them and kept under military guard, but the old court continued to meet and decide cases alongside of the new. The next electoral campaign found the people in more sober mood. The "Old Court party" elected sixty members of the legislature against thirty-five of the "New Court party," and at the next election a majority of the Senate was secured and a bill was passed in December, 1825, over the veto of the governor, by which all the laws constituting the new court were repealed.[1] An act was passed in 1830 by which the Bank of the Commonwealth ceased to loan money, apparently for the reason that no one cared to borrow the sort of money which it issued. The Commonwealth of Kentucky had a share in some banks afterwards established, but it did not again attempt the folly of State management.

The State of Alabama had an experience with a bank of State which, according to Governor Jones, has subjected the

[1] Shaler, 178–84.

people to a permanent tax of nearly $1000 per day for taxation to meet the cost of the experiment.[1] An act was passed December 21, 1820, to incorporate the Bank of the State of Alabama, but it provided for a capital of $2,000,000, of which three-fifths was to be obtained by private subscriptions. Subscriptions were slow in coming and the difficulty was met by an Act of 1823, removing any limit upon the capital and providing that the State should furnish the whole. Various public funds were set apart to constitute a part of the capital, among them the proceeds from the sale of lands donated by Congress for schools, amounting to about $1,300,000, and the funds of the University of Alabama to the amount of about $500,000. These grants were only a beginning, and between 1832 and 1837 the State issued bonds to the amount of $13,800,000 for the increase of the capital of the bank and to enable it to resume specie payments.

The purpose of the founders of the bank was to distribute the bank money as evenly as possible among the people of the State and the original act stipulated that the loans be apportioned among the several counties in proportion to their representation in the General Assembly. Loans to a single individual or corporation were not to exceed $2,000, but this rule was not closely adhered to in loans to the president and directors. The president and twelve directors were chosen by the General Assembly and the choice of directors for the branch banks increased the number annually chosen to between sixty and seventy. Candidates for the assembly were compelled to promise their supporters liberal loans in case of election and to exact pledges from candidates for the directorships that the loans should be granted. One of the hotel keepers of Tuscaloosa succeeded in securing an election as director in 1832 and his hotel swarmed with members of the legislature and persons desiring to borrow money, who hoped to secure his support in the negotiation of loans. Four other hotel keepers

[1] Century, *Cheap Money Experiments*, 88.

realized that they were conducting business under a heavy handicap and secured their own election as directors in 1834. A director could not afford to refuse a discount requested by a member of the legislature and the discounts of the bank increased from $448,859 in 1826 to $20,642,473 in November, 1837. The circulation had swelled in the meantime from $273,507 to $6,676,050.

Those were "flush times" in Alabama and so complete was the intoxication of the people with the paper money craze that the General Assembly on January 9, 1836, passed an act abolishing direct taxation in the State and setting aside $100,000 of the bank money to defray the expenses of the State government. The crisis of 1837 led to an investigation of the discounts and it was found that over $6,000,000 were worthless. Confidence in the paper money, "supported by the faith and credit and wealth of the State," to use the favorite phrase of the champions of government paper money, suddenly collapsed and with it the whole structure of business and credit in Alabama. The General Assembly was hastily summoned in special session and authorized a loan to the people of $5,000,000 in bank money, which was increased by $2,500,000 in December; but the fever had run its course, the charters of the branch banks were repealed in 1842, and the charter of the State Bank was not renewed when it expired in 1845. The assets of the bank netted about $10,000,000 towards reducing the bonded debt to the State, but $4,000,000 was a dead loss, in addition to the public funds originally set aside for the use of the bank. The effect of their experiment with a bank of State upon the people of Alabama was indicated by the provision of the constitution of 1867, that "The State shall not be a stock-holder in any bank, nor shall the credit of the State ever be given or loaned to any banking company or association or corporation."

Mississippi had a similar experience. Two early experiments in State ownership with bad results did not deter the people from the establishment of the Union Bank of Mississippi in 1838 with a capital of $15,000,000. This capital

was to be raised by means of loans to be obtained from the directors and the loans were to be negotiated through bonds of the State for which the credit of the State was pledged. The first block of $5,000,000 in bonds was sold at par through Nicholas Biddle, president of the Bank of the United States. The bank management exercised the worst possible judgment in loans and advances and the bank ran its course within four years. Post notes were issued, on account of the suspension of specie payments, and the issues of the bank and its six branches had increased in April, 1840, to $3,337,665. The other banks vied with the Union Bank in the issue of currency and at the close of 1839 the twenty-six banks in the State professed to have a paid up capital of $30,379,403, loans and discounts of $48,333,728 and a circulation of $15,171,639. As the free white population of the State at that time was only 170,000, the alleged paid-up capital equalled $180 per capita, loans and discounts $285, and circulation nearly $90. The State repudiated her obligations on the bonds issued and never attempted to pay them. The results upon the community are thus set forth by Mr. Henry V. Poor :[1]

> The $48,000,000 of loans were never paid ; the $23,000,000 of notes and deposits never redeemed. The whole system fell, a huge and shapeless wreck, leaving the people of the State very much as they came into the world. Their condition at the time beggars description. Society was broken up from its very foundations. Everybody was in debt, without any possible means of payment. Lands became worthless, for the reason that no one had any money to pay for them. The only personal property left was slaves, to save which, such numbers of people fled with them from the State that the common return upon legal processes against debtors was in the very abbreviated form of "G. T. T.," *gone to Texas*,—a State which in this way received a mighty accession to her population.

Several other Southern and Western States went through similar experiences. The Union Bank of Florida, chartered by the territorial government on February 12, 1833, with a capital of $1,000,000, was assisted by the issue of State bonds,

[1] *Money and Its Laws*, 540.

of which more than half were sold in Europe. The proceeds were loaned on stock and mortgages, mainly to stockholders, and the circulation was run up in 1839 to $551,747. A committee of the legislature made an investigation in 1840 and their report was very unfavorable to the bank. The State government, after the admission of Florida to the Union, refused to recognize the privileges of the Union Bank and the Secretary of State reported in 1858 that its circulating notes were worth not more than twenty cents on the dollar. A real estate bank was one of the features of the Arkansas system, towards which the subscribers to the stock were required to pay nothing in, but merely to secure their subscriptions by mortgaging their real estate. The working capital of the institution was obtained by the issue of State bonds, of which $2,000,000 were authorized. "A prudent expansion of the currency of the State" was one of the avowed objects of the bank and loans were made within a year after opening on December 12, 1838, amounting to $1,585,190. The circulation of the bank at this time was only $156,910, but specie payments were suspended and circulation was increased in May, 1840, to $759,000. The notes suffered a discount of forty to forty-five per cent. and it was soon discovered that the collection of loans on maturity was a far different matter from making them. The directors made an assignment on April 2, 1842, and the notes of the bank afterward passed for about twenty-five per cent. of their face value in specie. A like experiment had been going on in the meantime with the Bank of the State of Arkansas and the total amount of unredeemed bonds issued by the State on behalf of both banks, including interest, up to October 1, 1868, was $4,993,503.

Illinois tried several experiments at issuing money upon "the credit of the State," and the circulation of the State Bank of Illinois, incorporated in 1821, did not exceed $300,000. Even this moderate limit did not keep the notes from falling within three years to twenty-five cents on the dollar, and in 1825 an act was passed requiring the cashier of the bank to collect all the signed and unsigned notes in his pos-

session and burn them in the public square of Vandalia, in the presence of the governor and the judges of the Supreme Court. The next State Bank was incorporated in 1835 and $2,000,000 of the capital subscribed by the State was paid by the issue of bonds, which were taken by the bank at par. Assistance was also given to the Bank of Illinois at Shawneetown, but both banks collapsed in 1842 and the State was saved from much actual loss by the surrender by the banks of the State stock, which was burned in the Capital Square at Springfield in the presence of the legislature. The Constitution of 1848 provided that no State bank should thereafter be created nor should the State own any banking stock. Tennessee authorized a State Bank in 1820, which issued $1,000,000 in inconvertible notes in loans of $500 each upon real estate mortgages worth double the amount.[1] The notes quickly dropped below par and the bank closed in 1832.

Louisiana incorporated the Union Bank of Louisiana in 1832 upon similar principles with those of the Union Bank of Florida and issued $7,000,000 in State bonds to provide the capital. Bonds to the amount of $10,004,000 were issued to two other institutions, but all three failed in 1842 and the State enacted a sound banking law, under which she became in 1860 the fourth State in the Union in banking capital and the second in specie holdings.[2] The essential feature of the law was the requirement that the liabilities be covered one-third by specie and the remaining two-thirds by commercial paper having not more than ninety days to run. Louisiana prohibited State subscriptions for bank stock in her constitution of 1852. Georgia, Vermont, Missouri, Delaware and the Carolinas all tried State ownership and management of banks, but the first two early abandoned the experiment. The others ceased to be banks of issue with the establishment of the national banking system. The Farmers' Bank of Delaware was never much under political influences and is still conducted as a bank of discount and deposit. The Bank of Missouri had a coin reserve of one-third of its cir-

[1] Knox, *Rhodes's Journal of Banking*, Oct., 1892.

[2] White, *Sound Currency*, Vol. II., No. 1, p. 5.

culation and its connection with the State ended in 1866 by the sale of the State stock.

The State Bank of Indiana stands out, in the language of Mr. Horace White, a "notable tribute to sound banking principles from the weltering mass of bank failures of the period covered." The first bank of State was created originally as a private institution and adopted by the constitution of the State upon her admission in 1816 as a public bank. The experiment was a failure and it was not until 1834 that the State Bank of Indiana was incorporated, with ten branches. The parent bank, with a president and five directors elected by the legislature, acted as a sort of board of control over the branches, each of which was organized with a capital of $160,000 and chose one director as a part of the board of control. The two essential differences between the Bank of Indiana and the other banks of State were the payment of the capital in actual cash and the issue of notes upon liquid assets. The State, which took half the capital of each branch, paid its proportion in silver and advanced five-eights of the private capital by the sale of five per cent. bonds in London, taking mortgage security for the final payment by the shareholders and crediting them with the dividends paid by the bank. The remaining three-eights of the private capital was paid in cash by the shareholders, and each shareholder was made liable for an amount equal to his stock and the branches were jointly liable for each other's debts. The bank had a circulation in 1839 of $2,951,594.

The State Bank maintained a high credit, but was unable to obtain the renewal of its charter upon its expiration in 1857 because of a provision in the new constitution of 1851 that "the State shall not be a stock-holder in any bank after the expiration of the present bank charter." The State realized profits of $3,500,000 on the $1,000,000 invested in the institution, and its management had done so much for the development of the State that special privileges were given to a new State Bank of Indiana which was chartered March 3, 1855. The act of incorporation was quietly carried

through by a syndicate of politicians, who became large subscribers to the stock of the various branches. They opened negotiations with the managers of the old bank for the sale of the franchises and the latter made the purchase upon the condition that Hugh McCulloch, who had been for twenty years manager of the old Fort Wayne branch, should be made the president. The bank weathered the crisis of 1857 without suspending specie payments and rapidly retired its circulation when gold went to a premium in 1862. The bank was required by the conditions of its charter to pay its notes in coin, but a decision was obtained from the Supreme Court of the State that the United States legal tender notes were lawful money and could be lawfully used for the redemption of the notes. The circulation was reissued upon this basis, but upon the imposition of the ten per cent. tax on the circulation of State banks the State Bank of Indiana wound up its affairs with ample assets and unimpaired credit.[1]

The suspension of specie payments at the outbreak of the Civil War drove gold and silver from circulation and required an expansion of bank-note issues to maintain the volume of the currency. The Suffolk system continued in operation at Boston, but the notes failed to flow in as rapidly as before for redemption. The fact was noted and commented upon by the reports of the bank commissioners of Maine, New Hampshire and Massachusetts in their annual reports at the close of 1862 and among the reasons assigned was the fact that "in the present unsettled state of public affairs, the people have more confidence in the bills of the local banks than in any other paper currency."[2] Other reasons suggested were the large sums carried by soldiers to the seat of war and other sums left to be expended by their families, and the large amount of Eastern bills sent to the West by

[1] McCulloch, Ch. xi.–xii.

[2] Report of the Bank Commissioners of Maine, December 8, 1862, in *Annual Report of the Secretary of the Treasury on the Condition of the Banks of the United States at the Commencement of the Year 1863*, p. 3.

New York banks, to fill the gap created by the winding up of local institutions. The bank commissioners of Massachusetts maintained that when specie payments are suspended, "and bills are no longer redeemable in gold, a great motive for sending them home is withdrawn, since, if in good credit, they are as valuable as anything which can be got in exchange for them. Men hold them and hoard them, therefore, precisely as they would do with specie, and the volume of the currency becomes greater precisely as its current grows more sluggish."

It was very generally feared that the banks would sell their gold at a profit as it attained a high premium over legal tender paper, but the New England banks generally held on to their specie as a provision for the protection of their creditors and as security for future resumption. The commissioner of Maine reported, regarding the sale of specie for a premium, that "No instance has come to our knowledge where any bank has done anything of this kind; and certainly it cannot have been practised to any great extent, for the comparative tables show that, notwithstanding the suspension act, the specie in our banks has decreased only some $40,000." The New Hampshire commissioners reported that "the banks have not only kept their faith with the public, in retaining their specie in the vaults, but have actually increased the aggregate amount of specie, $38,827.52, or more than twelve per cent." The Massachusetts commissioners undertook to discourage sales of specie and declared that they "regard the sale of gold by the banks as altogether illegal, so long as they refuse to pay specie on their obligations."

One of the disadvantages of issuing bank-note circulation on securities was disclosed at the outbreak of the war in the sudden fall in value of Southern State bonds pledged by Northern banks to secure their circulation. This shrinkage in the value of the security for the notes was especially felt in Wisconsin. The case of the Koshkonong Bank, whose stock amounted at par to $48,000, of which all but $3,000 was issued by Southern States, was one of the worst, but

was typical of many others. The net proceeds of the bonds, when sold in the New York market, were only $21,769 and afforded the billholders only fifty-four and three-fourths per cent. on the dollar against an apparently well secured circulation of $39,779. The Bank Comptroller of Wisconsin was compelled to call upon nearly all the banks to make good the depreciation of stocks and their position became so precarious that a joint resolution was passed by the legislature on February 15, 1861, suspending further calls for additional securities. The Comptroller declared that "a general failure, involving three-fourths of all the banks, was imminent unless relief in some shape was granted ; and there is scarcely any occasion for doubt but at least eighty out of the one hundred and nine then existing banks would have failed."

The resolution of February was rescinded early in April and another call was made upon the banks to bring up the value of their stocks. Thirteen banks failed to respond and resisted the action of the Comptroller in the courts. The stronger banks gradually replaced Southern securities by those of Northern States and continued business upon this basis until the establishment of the national banking system. A shrewd stock jobbing scheme was put in operation by some of the bankers in the meantime by buying up depreciated currency at a great discount and offering it to the Comptroller for redemption in the better class of bonds, which could then be sold at a handsome margin over the cost of the currency. The Comptroller refused to permit the withdrawal of bonds except in such a way as to leave the better bonds in the custody of the State as security for the remaining circulation, but he modified this policy when he found speculators holding on to the notes, in anticipation of their final redemption from the proceeds of the stock, and surrendered good and bad stocks in fixed proportions.[1]

The New England banks felt the pressure of the repudia-

[1] Report of G. Van Steenwyck, Bank Comptroller of Wisconsin, Madison, October 1, 1861. House Ex. Doc. 25, 37th Cong., 3d Sess., 190–94.

tion of Southern obligations, but they had been preparing for it. Deposits fell in Boston from $20,811,889 on October 8, 1860, to $17,176,778 on December 10th, and specie reserves fell on December 17th to $3,491,348,—far below the limit required by law. The whole amount of Southern indebtedness to the North was estimated by intelligent merchants in New York and Boston at $200,000,000, and a large part of it was lost by the breaking out of war.[1] The Boston banks, however, succeeded in restoring their specie reserves by March, 1861, to $5,601,871, and the manner in which the banks of the State met their losses is thus described by the bank commissioners:

> The system pursued by them for many years, of making an annual reservation of a portion of their yearly earnings, had in some measure protected them against unusual amounts of dishonored and worthless paper. By the bank returns on the last Saturday of October 1860, the net profits then on hand amounted to $6,360,539.11, or $9\frac{9}{16}$ per cent. of the aggregate banking capital of the Commonwealth. And we do not hesitate to express the opinion, based upon the examinations we have made during the past year, and from information specially obtained from other banks, principally in Boston, that, notwithstanding the losses which some banks must inevitably sustain, the whole amount of final loss growing out of our difficulties with the South will be more than covered by the general surplus, thus leaving the aggregate bank capital free and unimpaired.[2]

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[1] Some estimated it at $200,000,000 to New York alone.—Rhodes, III, 560. The honorable conduct of the New Orleans banks is pleasantly referred to by Secretary Hugh McCulloch. The branches of the Bank of Indiana in the southern part of the State, he says, "had large dealings with men who were engaged in the Southern (Mississippi) trade, and when measures were being instituted for the secession of Louisiana from the Union, and, indeed, after the ordinance of secession had been adopted, these branches had large cash balances and large amounts of commercial paper in the New Orleans banks. Against the remonstrances of the secession leaders, and in disregard of threatened violence, these cash balances and the proceeds of the commercial paper as it matured were remitted for according to directions,—not a dollar was withheld."—*Men and Measures of Half a Century*, 139.

[2] House Ex. Doc. 25, 37th Cong., 3d Sess., 50.

The growth of the capital and business of the State banks of circulation is shown in the following table:

YEAR.	NO. OF BANKS.	CAPITAL STOCK.	LOANS AND DISCOUNTS.	DEPOSITS.
1834	506	$200,005,944	$324,119,499	$ 75,666,986
1835	704	231,250,337	365,163,834	83,081,365
1836	713	251,875,292	457,506,080	115,104,440
1837	788	290,772,091	525,115,702	127,397,185
1838	829	317,636,778	485,631,687	84,691,184
1839	840	327,132,512	492,278,015	90,240,146
1840	901	358,442,692	462,896,523	75,696,857
1841	784	313,608,959	386,487,662	64,890,101
1842	692	260,171,797	323,957,569	62,408,870
1843	691	228,861,948	254,544,937	56,168,628
1844	696	210,872,056	264,905,814	84,550,785
1845	707	206,045,969	288,617,131	88,020,646
1846	707	196,894,309	312,114,404	96,913,070
1847	715	203,070,622	310,282,945	91,792,533
1848	751	204,838,175	344,476,582	103,226,177
1849	782	207,309,361	332,323,195	91,178,623
1850	824	217,317,211	364,204,078	109,586,595
1851	879	227,807,553	413,756,799	128,957,712
1853	750	207,908,519	408,943,758	145,553,876
1854	1,208	301,376,071	557,397,779	188,188,744
1855	1,307	332,177,288	576,144,758	190,400,342
1856	1,398	343,874,272	634,183,280	212,705,662
1857	1,416	370,834,686	684,456,887	230,351,352
1858	1,422	394,622,799	583,165,242	185,932,049
1859	1,476	401,976,242	657,183,799	259,568,278
1860	1,562	421,880,095	691,945,580	253,802,129
1861	1,601	429,592,713	696,778,421	257,229,562
1862	1,492	418,139,741	646,677,780	296,322,408
1863	1,466	405,045,829	648,601,863	393,686,226

Tradition has handed down unhappy memories of the State banks, which have been distorted by the lapse of time into conceptions very different from the facts. The several systems, taken in the aggregate for the entire country, had the great practical defect of lack of uniformity. This defect was great enough to obscure the essential merits of many of the State systems and to make any system which was national in its scope and uniform in its character attractive to the business community of the whole country. Whatever the merits or defects of the State systems, the currency in circulation was judged by the worst of the systems, for by the operation of Gresham's law that currency tended to drive

out of circulation all kinds which were superior; and even where this was prevented by laws or local conditions, the bad currency was a constant source of irritation from the very necessity of discriminating, in receiving money payments, between the bad and the good. One of the requirements of the modern business world is undoubtedly a uniformity of currency which shall obviate the necessity for discrimination and make every dollar of equal exchange value with every other. This condition was not met by the aggregate of State currencies and the fact that it was fully met by the New England currency at its best may easily have been obscured, in the minds of New Englanders, by the multiplicity of good and bad currencies from other sections which caused perpetual inconvenience.

The national banking system of later years garnered up the lessons of many experiments with banking upon securities, adopted most of the good and discarded most of the bad features, and afforded the country two of the great benefits of a sound currency,—security and uniformity. The necessity of discrimination between currencies ceased when every dollar in circulation rested upon a common basis,—the credit of the national government. The necessity of paying high exchange rates, or surrendering the notes of distant banks at a heavy discount, ceased also when every note became as good in one part of the Union as in another. Coupled with these great benefits of the new system was the feature of Federal supervision and examination, which arrested the creation of fraudulent banks at the outset and subjected them annually or oftener to the power of visitation by the national authority. The three great benefits,—security, saving of exchange, and Federal supervision,—are almost inherent parts of a national system. The fact that they have been associated with a particular national system has led many to believe that there can be no other equally good, and that enmity to the present banking law is enmity to the principles of sound finance. But all these benefits can be obtained under national law with the added benefits, which the present system lacks, of a banking currency ample

for the demands of business, without the help of government paper money, and flexibly responsive to those demands.

The foundation of a national currency upon evidences of public debt is dangerous and unscientific and proved fatal to some of the State currencies before the Civil War. A comparison of the State systems shows a distinct line of cleavage which is far from favorable to the principles of the present national banking law. This line of cleavage separates the banks issuing currency against general assets, like those of New England, Indiana, and Louisiana, from those issuing circulation, on the other hand, against securities, like the banks of New York, Illinois, and Wisconsin, and those established under the parental care of the State, like the Bank of the Commonwealth of Kentucky, the Union Bank of Florida, the State Bank of Alabama, and the Bank of Mississippi. The experience of the New England and Indiana banks is the triumphant vindication of the principle of banking on general assets and issuing notes redeemable in coin on demand, which is supported by the critics of the present national system and the advocates of a banking currency. The banks issuing circulation on securities, with their pitiable failures and their wildcat banking, were the prototypes of the national system and afford a hint of what that system would become if note issues based upon State and municipal securities were substituted, as is sometimes proposed, for note issues based upon national bonds. It must be remembered, moreover, that perfect as the security seems for bank-notes under the national system, it is a security which has followed the ups and downs of government paper money. There was neither purpose nor pretence of maintaining the notes of national banks at parity with coin while the notes of the government itself and the bonds by which bank-notes were secured were depreciated. Bank-notes remained from 1864 to 1879 at par with government obligations because those obligations themselves were far below par in coin.

If the banks issuing circulation upon securities were the model for the national banks of to-day, the banks of State

which existed before the war were the models and the prototypes of the Federal treasury management under the *régime* of legal tender paper. Their issues were not bank-notes in the sense in which banking currency is opposed to a government paper currency, but they were simply the bills of credit of the State resting upon the credit of the State as completely as the paper roubles of the Bank of Russia. The fact that they were hardly ever maintained at par in coin, in spite of the great wealth and undoubted honesty and good faith of the people of the various commonwealths, is a practical demonstration of the folly of attempting to do a banking business upon general credit without quick assets. The lesson of the history of the State banking systems, reduced to its simplest terms, is the success of the systems based upon the banking principle and the failure of the systems based upon the deposit of securities, like the national banking system, or based simply upon the public credit, like the government currency system of the United States.

One of the essential errors of early banking in the United States was the undue expansion of credit upon slender resources. It is an error common in a new country and one from which the United States and Australia, in more recent years and under other systems of note issue, have not been exempt. The impression has been assiduously cultivated by the opponents of a banking currency that the early American banks issued a volume of circulating notes enormously in excess of the legitimate demands of business. This impression is absolutely unfounded and the proof is afforded by the figures. Some of the State banking currencies were over-issued in the sense that every dollar which is not kept at par with the metallic standard is improperly issued, but the aggregate banking currency of the country was at no time over-issued in the sense that an equal volume of good money was not capable of ready and healthy absorption by the legitimate demands of business. The circulation of all forms of money in the United States between 1880 and 1895 has ranged between $21.71 and $24.44 and has only

recently been regarded, with the slackening of business activity, as beyond the volume required by business needs. It is only necessary to compare such figures with those of the circulation prior to the Civil War to show how erroneous is the assertion that the currency was unduly inflated in volume during the years of State banking. The following table shows the circulation of both bank-notes and specie at various dates, including the years of largest circulation,—the difference between the bank-note circulation and the total money in circulation representing the specie:

YEAR.	ESTIMATED BANK-NOTES OUTSTANDING.	TOTAL NOTES AND MONEY IN CIRCULATION.	POPULATION.	CIRCULATION PER CAPITA.
1800	$ 10,500,000	$ 26,500,000	5,308,483	$4.99
1810	28,000,000	55,000,000	7,239,881	7.60
1820	44,800,000	67,100,000	9,633,822	6.96
1830	61,000,000	87,344,295	12,866,020	6.69
1835	103,692,495	145,799,637	14,786,000	9.86
1837	149,185,890	217,185,890	15,655,000	13.87
1840	106,968,572	186,305,488	17,069,453	10.91
1845	98,608,711	177,950,405	19,878,000	8.95
1850	131,366,526	278,761,982	23,191,876	12.02
1853	188,181,000	402,238,107	25,615,000	15.80
1854	204,689,207	425,551,240	26,433,000	16.10
1855	186,952,223	418,020,247	27,256,000	15.34
1856	195,747,950	425,846,625	28,083,000	15.16
1857	214,778,822	457,068,708	28,916,000	15.81
1858	155,208,344	408,810,028	29,753,000	13.78
1859	193,306,818	438,967,542	30,596,000	14.35

CHAPTER XV.

THE NATIONAL BANKING SYSTEM.

State of the National Finances at the Beginning of the War—The Suspension of Specie Payments and the Loan Policy of Secretary Chase—The First Plans for the National Banking System—Changes in the Circulation—The Necessity for a New System and the Plan of Secretary Carlisle—Recommendations of Comptroller Eckels.

THE national banking system of the United States had its origin in the management of the finances during the Civil War. The system was hardly in operation until the war was two-thirds over, but it offered a market for the public securities which contributed materially to raise their price in the depreciated paper with which the government discharged its obligations. The system afforded the country for some years a currency having the advantages of uniformity and security, and possessed in these respects a great advantage over the bank currency of the different States which had before been in use. The national banking system, however, great as were its services in absorbing the evidences of the public debt, always lacked the essential feature of a purely banking currency. The currency was without elasticity, in the sense of responsiveness to the demands of business, and the volume fluctuated only with the price of securities. The gradual reduction of the public debt has removed the basis for national bank-note circulation until it has become but a trifling factor in the currency system of the country, and a strong demand has arisen for the separation of the note issues from public securities.

The United States at the outbreak of the Civil War were conducting their financial operations through the independent Treasury. The notes of the State banks formed a large part of the medium of exchange in private transactions, but only specie was accepted in payments to the government. The aid of the banks was not sought in handling funds, in making transfers, in placing loans, or in paying interest. This at least was the theory of the independent Treasury, although in fact the absence of proper depositaries led many public officers to deposit their funds temporarily in the banks at their own risk.[1] The circulation of the country outside of the Treasury on July 1, 1861, consisted of $246,400,000 in specie and $202,005,767 in the notes of State banks, making a total of $448,405,767, or $13.98 per capita.[2] The essential question for Mr. Chase, Lincoln's Secretary of the Treasury, was whether the operations of a great war could be carried on through these instrumentalities. The question was the occasion of much discussion at the time and has never been answered to the satisfaction of all sides. The answer of Mr. Chase was that the operations of the war could not be carried on upon a basis of specie and State bank paper.

The government was obliged almost at the outset to abandon the position that it was able to carry on its own finances without the help of the banks. Some small loans had been placed by public subscription during the administration of Buchanan, but it was perfectly obvious that great sums could not be obtained quickly except from the banks, which had the keeping of the transferable capital of the country. Secretary Chase held a conference in New York on August 9, 1861, with representative bankers of New York, Philadelphia, and Boston. They agreed to advance to the Treasury $150,000,000 in gold, to be secured by three-year notes bearing interest at 7.30 per cent., and to be reimbursed as the proceeds of the sale of bonds were covered into the Treasury. This union of the banks of New York, Boston, and Philadelphia in support of the public credit was one of the most

[1] Kinley, 60–61.

[2] *Finance Report*, 1894, p. cviii.

important events of the war and committed the conservative business element conclusively to the side of the Union and the policy of coercion of the seceded States. The banks of the three big Eastern cities had an aggregate capital of $120,000,000, a circulation of $16,964,749, deposits of $125,-617,207, and coin reserves of $63,165,039, the latter being equal to forty-five per cent. of demand liabilities.[1] They had already made an agreement in November, 1860, when secession compelled them to contract their business and prepare for a period of stress, for issuing clearing house certificates and making the specie of all the banks available as a common fund.[2]

Congress passed an Act on August 5, 1861, relaxing the provisions of the sub-treasury law so far as to permit the Secretary of the Treasury to deposit any money obtained from loans to the credit of the United States Treasurer in such solvent specie-paying banks as he might select.[3] The banks accepted this law as authority for the use of the ordinary means of commercial exchange,—bank-notes, checks and drafts,—in the transactions of the government. They recommended to the Secretary, therefore, that he should take the proceeds of the advances made by the banks by drawing checks and drafts upon the banks, in favor of public creditors. They suggested that this would not only prove of great practical convenience, but would diminish the hoarding which would take place if the banks paid out their coin and reduced their reserves while uneasiness as to the future prevailed in the business community. Secretary Chase, to the surprise of nearly every financier, declared that the Act of August 5th had no such meaning or intent and that he should require payment of the advances in coin. The subject was warmly discussed between the Secretary and the bankers, but the Secretary's purpose was unshaken and the banks yielded rather than break off negotiations so important to the maintenance of the public credit.

[1] Poor, 557.
[2] Bolles, III., 23.
[3] Acts of Thirty-seventh Congress, 1st Sess., Ch. 46, Section 6.

One of the acts of the special session of Congress in the summer of 1861 authorized loans in several forms, including non-interest bearing notes of denominations less than $50, payable on demand by the assistant treasurers at New York, Boston, and Philadelphia. These notes were not made legal tender and Secretary Chase, in recommending them, declared that "The greatest care will, however, be requisite to prevent the degradation of such issues into an irredeemable paper currency, than which no more certainly fatal expedient for impoverishing the masses and discrediting the government of any country can well be devised." Notwithstanding this brave language, the Treasury began to issue the new notes early in August. They were very reluctantly accepted as currency and the banks refused to receive them except as special deposits. The new notes threatened to bring infinite disorder into the currency system by the element of inflation which they involved. The banks filed a prompt protest against thus trifling with the circulating medium while they were straining their resources to withdraw capital from active industry and divert it to the uses of the government. The Secretary intimated that he would suspend the issue of such notes until other resources were exhausted, but that he did not regard it as proper to pledge himself openly not to exercise a power conferred by law.

This was before the advances by the banks had begun, and upon this assurance they began to pay coin into the sub-treasury at the rate of about $5,000,000 at intervals of six days. The attempt to secure popular subscriptions for the seven-thirty notes through the agents of the government resulted in subscriptions of only $24,678,866, and the banks themselves came forward and took the notes and agreed to negotiate their distribution among the people. So perfect was the public confidence in the associated banks and so rapid the circulation of the money that the specie in the banks had not been materially reduced after the payment of the second instalment. The gold paid by the banks into the sub-treasury was disbursed by public officers and through the channels of circulation found its way back into

the banks. There was no apparent reason why advances should not be made in this manner to meet all the demands of the war without impairing the solvency of the Eastern banks. Fears were expressed in some quarters that the coin would gradually be absorbed by the Western banks, some of which were on a rather shaky foundation and had issued notes secured by the bonds of the seceded States. This evil had not begun to operate, however, before Secretary Chase again began to put in circulation a mass of demand notes issued directly by the government.

The Secretary did not long respect his assurances to the banks. The promise was given in August and heavy issues of notes took place in November. They were not cordially received as a means of circulation and were largely presented to the sub-treasuries for redemption in coin. The Treasury had little coin except that drawn from the banks, and the coin reserves of the latter now began to decline without any signs of recuperation. The specie in the New York banks, which was $49,733,990 on August 17th and $42,318,610 on December 7th, fell to $29,357,712 on December 28th. A conference was held with Secretary Chase and he was assured that the Treasury notes could not be received by the banks at par with coin and that their steady infusion into the currency would send gold to a premium as well as create an inflation of the paper circulation which would drag down the value of bank-notes in the same manner as the Treasury notes. The Secretary stubbornly refused to change his policy and the banks voted to suspend specie payments on Monday, December 31st.[1] The government necessarily followed

[1] Prof. Sumner seems to ignore the effect of the government issues of the demand notes and declares that the banks suspended, "without any earnest attempts to avoid it, and certainly without any necessity." —*History of American Currency*, 194. Secretary Chase, on the contrary, did not appear to blame the banks, but declared that unexpected military delays had increased expenditures, and diminished confidence in public securities, and that "These conditions made a suspension of specie payments inevitable."—*Report on the Finances*, 1862, 7.

suit, for the independent Treasury afforded no adequate fund of coin for keeping afloat such a mass of paper as Mr. Chase proposed to put into circulation.

This suspension, less than six months after the first serious conflict at Bull Run, opened the way for the long experience of irredeemable paper currency which ended only with the resumption of specie payments on January 1, 1879. The legal tender notes, which followed quickly on the heels of the demand notes, changed the standard of value in the United States, drove gold across the ocean or into private hoards, deprived us of foreign help and sympathy,[1] advanced prices from one hundred to two hundred per cent., and added enormously to the profits of speculators and to the costs of the war to the people of the country. The price of gold advanced steadily from the suspension of specie payments until the summer of 1864, when it touched 285. The wholesale prices of nearly all articles climbed upward with the gold premium and retail prices in many cases advanced still more, increasing the paper cost of every contract for carrying on the war. The government was obliged to sell its securities for depreciated paper, and to apply the proceeds to settlements in the same inflated medium. A computation of the proceeds of $2,565,233,591 received from the sale of public obligations for paper currency during forty-five months ending September 30, 1865, put the gold value at $1,705,347,632, representing a loss to the government by its depressed credit of $860,000,000, or more than the entire bonded debt left in force at the beginning of the fiscal year 1889.[2]

There have always been those who have maintained that the suspension of specie payments was a necessary condition

[1] In the case of America there was a further evil ; being a new country, she ought in her times of financial want to borrow of old countries ; but the old countries were frightened by the probable issue of unlimited inconvertible paper, and they would not lend a shilling.—Bagehot, *The English Constitution*, Ch. i., Works, IV., 46.

[2] H. C. Adams, "American War Financiering," *Pol. Sc. Q'rly.*, September, 1886, I., 374.

of war. The managers of the associated banks of the East recognized no such necessity until Secretary Chase began to flood the country with government paper money for which he had no means of redemption. They pointed out that transactions to the amount of $20,000,000 were settled daily in New York, without coin or even notes and that the settlement of an additional one or two million dollars daily for the government could be easily effected by the same machinery. It was only necessary that the government should have in hand at any one time enough currency, even if it insisted upon coin, for the transactions of a few days, while the means of giving mobility to the capital and resources of the country constantly existed in the hands of the banks. When the Secretary showed himself immovable upon the subject of issuing irredeemable notes, the suggestion was made to him that, if this dangerous path must be trod, it could be done much more safely through the banks than directly through the Treasury. In the forcible language of Mr. George S. Coe, it was represented to Mr. Chase: [1]

> That if an irredeemable paper currency was the inevitable resort, it would be more expedient and economical for the government not to become involved in its dangers, but to impose the duty and responsibility of issuing the notes upon the banks, who would naturally be compelled to keep the day of redemption continually in view. Thus, as a suspension of coin payment was about to be declared, it was practicable to preserve from distribution and set aside the forty millions of coin then owned by the banks, together with one hundred and fifty or sixty millions of government bonds, which could be taken by them as a special security for two hundred millions of notes, which could then be immediately issued by the associated banks from their own plates, and be verified and made national by the stamp and signature of a government officer. And that such an issue, so supported by coin and bonds, at once simple and expeditious, would serve the temporary purpose required, with little if any deterioration below coin value; and that it would be then practicable for the banks to continue, without further agitation, their advances. But the Secretary declined to entertain this suggestion; preferring the system of national banks which he had already conceived.

[1] "Financial History of the War," *Bankers' Magazine*, Jan., 1876.

Secretary Chase made the fatal mistake at the outset of relying upon loans to supply the means of carrying on the war instead of appealing to the productive resources and the patriotism of the people. His recommendation, at the special session of Congress in the summer of 1861, was to raise $80,000,000 by taxation and $240,000,000 by loans. Of the amount raised by taxation $65,000,000 was required for the ordinary expenses of the peace establishment, $9,000,000 was to pay the interest on the new debt, and $5,000,000 was to go to the establishment of a sinking fund for its final payment. It is no afterthought to declare that this policy of timidity was not approved by the country. A meeting of bank delegates was held in Washington on January 11, 1862, which recommended a tax bill to raise $125,000,000 in addition to the usual duties on imports. A resolution was introduced in the House four days later declaring in favor of an annual revenue of $150,000,000. This resolution passed the House with only five dissenting votes, and its beneficial effect was shown by the advance of six per cent. bonds from 90 to 107. The New York Chamber of Commerce, on April 24th, adopted a memorial to Congress declaring "that the masses of the people are ready and desirous to contribute their quota to the ordinary and extraordinary revenues of the country," and that the public expenditures demanded an annual revenue of at least $250,000,000.

It was not until his annual report of 1863 that Secretary Chase awakened to the importance of taxation as a means of supporting the public credit, and suddenly expressed his desire for providing "for the largest possible amount of extraordinary expenditures by taxation." The net ordinary receipts, exclusive of loans, were $51,919,261 for the fiscal year ending June 30, 1862; $112,094,945 for the fiscal year 1863; $243,412,971 for 1864; $322,031,158 for 1865; and $519,949,564 for 1866. If these figures could have been moved backwards a single year, the effect upon the credit of the government, the price of gold, and the depreciation of the legal tender paper would have been striking, even

if the change had not made it unnecessary to depart from the metallic standard. It is probable that of the $6,344,371,435 computed[1] as the cost of the war up to the resumption of specie payments in 1879, $2,000,000,000 could have been saved to the tax-payers and the public debt would no longer exist. Outside and beyond these considerations, moreover, was the injury done to depositors in savings banks and to other creditors by payment in a depreciated dollar, and the injury to laborers, whose wages were far from keeping pace with the advance in paper prices.[2]

It has been necessary to refer to the financial policy of Secretary Chase in order to show the conditions out of which grew the national banking system. The system was a part of the Secretary's policy of carrying on the war by means of loans, and was intended to make a market for American securities and to maintain their price. One of the first effects of the suspension of specie payments was the increase of the

[1] Bolles, III., 244. Mr. Edward Atkinson computes the war expenditures for the seven years, 1862 to 1868, exclusive of the peace establishment, at $4,150,000,000, of which "not less than $2,200,000,000 was paid for war material and supplies, the prices of which were raised by the depreciation of bad money." The average advance in prices in the four years of war over the prices of 1860 was 87 per cent., which increased the cost of material of war $1,000,000,000. Since that time we have paid more than five per cent. interest for thirty years on seven-tenths of this sum, amounting to $1,050,000,000. —"The Cost of Bad Money," *Harper's Weekly*, Oct. 12, 1895, XXXIX., 964.

[2] Wholesale prices followed the gold premium in a majority of cases at once or at an interval of about a month, but the advances in many retail lines were undoubtedly much more rapid. Wholesale prices, moreover, remained stationary for nearly a year after the gold premium began to fall, and then only followed it downward at long removes. See the admirable article of Fred Perry Powers, "The Greenback in War," *Pol. Sc. Q'rly*, March, 1887, II., 79. Mr. Atkinson, in the article quoted above, computes the transfer of profits from wage earners to speculators or capitalists, as the result of the legal tender laws, at $7,000,000,000 in the seven years 1862–68,—$40 per head annually, or $120 for a family of three, exclusive of enhanced payments directly for taxes, out of an average income of about $450 per family.

circulation of the existing banks. The banks were very prudently conducted when the war cloud first threatened, but they were soon confronted by a real demand for additional circulation to take the place of the gold which disappeared with the suspension of specie payments. The circulation of the country outside the Treasury, which had been $448,405,767 on July 1, 1861, had declined to $334,697,744 on July 1, 1862. The entire mass of specie in circulation on the earlier date, which was $246,400,000, had disappeared, except about $25,000,000 on the Pacific Coast. United States notes and demand notes had been pumped into the circulation to the amount of $125,905,665, but they did not fill the void left by the flight of gold and silver. The scarcity of currency was more than remedied by July 1, 1863, when the total had been swelled to $595,394,038, of which $312,481,418 was in United States notes and $238,677,218 in the notes of the State banks. The circulation of the latter had increased about $53,000,000 within the year.

Secretary Chase inquired in his first annual report in the autumn of 1861 whether, as the bank-note circulation constituted a loan without interest from the people to the banks, sound policy did not require that the advantages of this loan be transferred, in part at least, from the banks, representing only the interest of the stock-holders, to the government, representing the aggregate interest of the whole people. The Secretary suggested that Congress had power to control the credit circulation, and that circulating notes might be issued under national authority and secured by the pledge of United States bonds. He outlined the advantages of his proposed measure thus:

> Its principal features are, (1st) a circulation of notes bearing a common impression and authenticated by a common authority; (2d) the redemption of these notes by the associations and institutions to which they may be delivered for issue; and (3d) the security of that redemption by the pledge of United State stocks, and an adequate provision of specie.
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> In this plan the people, in their ordinary business, would find the

advantages of uniformity in currency; of uniformity in security; of effectual safeguard, if effectual safeguard is possible, against depreciation; and of protection from losses in discounts and exchanges; while in the operations of the government the people would find the further advantage of a large demand for government securities, of increased facilities for obtaining the loans required by the war, and of some alleviation of the burdens on industry through a diminution in the rate of interest, or a participation in the profit of circulation, without risking the perils of a great money monopoly.[1]

The Committee of Ways and Means of the House of Representatives set to work upon a bill and made a careful study of the banking laws of the various States. The Secretary's scheme was based upon the New York free banking law and had been urged upon Mr. Chase as early as August, 1861, by Mr. O. B. Potter of that State. Some improvements on the New York plan were incorporated in the bill of the committee. The provisions relating to the reserve fund were drawn largely from the banking laws of Louisiana, and other features were adapted from the laws of Ohio and Illinois. It was pointed out early in the public discussion of the plan that the volume of circulation would depend upon the price of bonds rather than upon the needs of the money market, and opposition was pronounced among the New York bankers. Thaddeus Stevens reported against the bill, and its necessity was postponed for the time being by the issue of legal tender notes. Mr. Chase returned to the subject in his annual report for 1862, and his language in favor of basing the monetary circulation on evidences of the public debt sounds very like that adopted by Mirabeau, in urging the issue of the *assignats* upon the French Assembly.[2] The Secretary declared:

Every dollar of circulation would represent real capital, actually invested in national stocks, and the total amount issued could always be easily and quickly ascertained from the books of the Treasury. These circumstances, if they might not wholly remove the temptation to excessive issues, would certainly reduce it to the lowest point, while the form of the notes, the uniformity of devices, the signatures

[1] *Report on the Finances*, 1861, 19.

[2] *Vide* Ch. xxiii.

of national officers, and the imprint of the national seal authenticating the declaration borne on each that it is secured by bonds which represent the faith and capital of the whole country, could not fail to make every note as good in any part of the world as the best known and best esteemed national securities.[1]

The time was more nearly ripe for such a device than in the preceding session, and a bill was promptly introduced in the House by Mr. Hooper of Boston, who had given much attention to the subject during the summer. Senator Sherman introduced a similar measure in the upper branch, which was passed and went to the House on February 12th. Much of the argument in the Senate was based upon the fact that the existing banks were increasing their circulation, without the restraining influence of specie payments, and were using the constantly swelling volume of government paper money as a means of redemption. The debate in the House was opened by Mr. Spalding of New York, who had enjoyed the doubtful honor of fathering the legal tender law. The bill passed the Senate by a vote of 23 to 21; passed the House on February 20th by a vote of 78 to 64, and received the signature of the President on February 25, 1863. The measure proved to be defective in some of its details, however, and was superseded by the Act of June 3, 1864. Banks to the number of 134 had been organized when the Comptroller of the Currency made his first report in November, 1863, but no notes appeared until late in December. The system was hardly in operation, therefore, until the war was within a year of its end, but the fact that it had been authorized undoubtedly contributed to create a market for securities and to maintain their price.

The essential feature of the new banking law, so far as concerns circulation, was the provision that circulating notes should be issued by the Comptroller of the Currency upon deposits of United States bonds, to the amount of ninety per cent. of the face value of the bonds. No bank could be organized with a less capital than $100,000, except in places with a population not exceeding six thousand, where a

[1] *Report on the Finances*, 1862, 18.

bank might be organized, with the approval of the Secretary of the Treasury, with a capital of not less than $50,000. At least fifty per cent. of the capital was required to be paid up before beginning business and the remainder in instalments of ten per cent. of the whole amount of the capital at the end of each month. The bond deposit was fixed at not less than $30,000 nor less than one-third the capital stock. Provision was afterwards made by the Act of June 20, 1874, for the withdrawal of circulating notes at the option of the banks and the surrender of an equivalent amount of bonds by the Treasury, provided that the amount of bonds on deposit should not be reduced below $50,000. The limit was further reduced in 1882, for banks having a capital of $150,000 or less, to one-fourth of their capital stock, but limitations were set upon both the retirement and the issue of new circulation. The withdrawal of currency was not permitted to proceed at the rate of more than $3,000,000 per month for the entire country, and a bank reducing circulation was not entitled to receive any increase for the period of six months from the time it made a deposit of lawful money, in lieu of the bonds, for the redemption of outstanding notes.[1]

The new banking currency was put upon the same depreciated paper basis as the bonds and legal tender notes of the government. It could not have circulated otherwise in common with United States notes, for it would have been at a premium, like gold, or would have been presented to the banks for redemption in gold for hoarding. The law made the notes redeemable in "lawful money." Redemption of this sort was simply the exchange of a note secured by one government obligation for another, and was of so little value that the banks were seldom troubled by the presentation of their notes, although they were required to carry large quan-

[1] This limitation proved troublesome to a few banks which desired to take out circulation quickly during the panic of 1893, but had within six months deposited lawful money with a view to retiring circulation. Comptroller Eckels recommended its repeal in his annual reports for 1894 and 1895.

tities of legal tenders as a part of their lawful reserve.[1] The banks in Albany, Baltimore, Boston, Cincinnati, Chicago, Cleveland, Detroit, Louisville, Milwaukee, New Orleans, New York, Philadelphia, Pittsburg, St. Louis, San Francisco, and Washington were required to keep a reserve in lawful money equal to twenty-five per cent. of their aggregate notes in circulation and deposits. Banks outside of these "reserve cities" were required to keep a reserve of at least fifteen per cent., but three-fifths of the reserve in these cases might be deposited with banks in the "reserve cities."

Hugh McCulloch was the first Comptroller of the Currency appointed under the new law, and it is to his ability and good judgment that much of the success of the new banking system was due. He had been president of the admirably managed Bank of the State of Indiana, and went to Washington in 1862 to oppose the national banking bill. His opinions underwent a change after the bill was amended in the following year and became a law, but it was with some surprise that he received the invitation to become the head of the new system. He stipulated for absolute control over the choice of his employees and for permission to resign the place as soon as the system was well organized. The First National Bank of Philadelphia was the first authorized to begin business, on June 20, 1863. Several other certificates were issued on the same day, but the Western banks were generally more prompt to come into the national system than those of the East. Mr. McCulloch discusses some of the objections to the new system and the manner in which he met them, in the following passage of his memoirs:

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[1] It was the distinct proposal of Secretary Chase that the notes should be payable, "after resumption, in specie, by the association which issues them, on demand; and if not so paid will be redeemable at the Treasury of the United States from the proceeds of the bonds pledged in security."—*Report on the Finances*, 1862, 17. But this safeguard was not adopted, and the banks continued, long after resumption by the Treasury, to redeem their notes only in paper money.

There were four causes for the unwillingness of the State banks to become national banks.

First: The apprehension that the national system might prove to be a repetition of the free-bank system of the West, which had been a disreputable failure.

Second: The opinion that in becoming national banks, and issuing notes secured by Government bonds, their interests would be so identified with the interests of the Government, their credit so dependent upon, so interwoven with, the public credit, that they would be ruined if the integrity of the Union should not be preserved.

Third: the danger of hostile legislation by Congress, or the annoyances to which they might be exposed by Congressional interference with their business for partisan purposes.

Fourth: The requirement, that in order to become national banks, they must relinquish the names to which they had become attached, and be known by numerals.

I had no great difficulty in satisfying the bankers with whom I had personal interviews or correspondence that three of these objections were unsubstantial. In answer to the first, I pointed out the important particulars in which the national system differed from the free-bank system of the West, in the requirement that the capitals of the national banks should be real, and fully paid up; that their circulation was to be secured by United States bonds, with ten per cent. margin; that in case of the failure of a bank, its notes would be at once redeemable at the United States Treasury; that all the banks would be subjected to frequent examinations by men appointed by the Treasury Department. In answer to the second, I took the ground that the interests of the State banks were already so involved with those of the Government, that the fate of the latter would be the fate of the former also; that whether they remained State banks or became national, they would stand or fall with the Government. In answer to the third, I expressed the opinion that there was as little to fear from Congressional as from State legislation; that if there was trouble to be apprehended in either direction, it would be in the control which the banks might have over Congress, rather than in annoying interference by Congress with their legitimate business. To the fourth I could make no reply. It seemed to me to be unreasonable that the State banks should be required, in order to be converted into national banks, to surrender the names that had been made honorable by the manner in which their business had been conducted, and accept for a name, a number.[1]

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[1] *Men and Measures of Half a Century*, 168, 169.

The last point was finally conceded by the Secretary, and banks were allowed to retain their old names with the prefix "national." When this was yielded, says Mr. McCulloch, "they came into the national system with a rush,—Boston, as is her wont in all enterprises, taking the lead." An Act was passed in 1873 forbidding the use of the word "national" in the titles of banking institutions not organized and transacting business under the National Currency Act.

The destruction of the State banks as banks of issue by taxation was not a component part of the national banking system at its origin. Secretary Chase, in his first annual report, suggested the possibility of taxation, in order to transfer to the government some of the profits of circulation, and he remarked, in his second annual report for 1862, that he had "heretofore advised the imposing of a moderate tax on corporate circulation, and now renews the recommendation as the best means of reduction and gradual substitution." The first banking act provided that any State bank holding United States bonds to the amount of fifty per cent. of its capital stock might deliver them to the United States Treasurer and receive circulating notes equal to eighty per cent. of the face value of the bonds transferred, and that upon the failure of such a bank the bonds should be declared forfeited to the United States and the circulating notes should be redeemed and paid at the United States Treasury. These provisions for State banks were omitted from the Act of June 3, 1864, and Comptroller McCulloch, in his annual report for 1864, suggested the query whether "the time has not arrived when all these institutions should be compelled to retire their circulation?" He stated that he had not felt like recommending such action "as long as there was any uncertainty in regard to the success of the national banking system," and he limited his recommendations to taxation "which should be sufficient to effect the object without being oppressive."[1] The result was a provision in the Revenue Act of March 3, 1865, laying a tax of ten per cent.

[1] *Report on the Finances*, 1864, 54.

per annum upon the circulation of State banks paid out by them after July 1, 1866. This provision, therefore, did not take effect until a year after the practical close of the war, and was intended to drive the State banks out of competition with the national system and to enlarge the market for United States bonds.

There was still in circulation on July 1, 1864, $179,157,717 in State bank-notes and only $31,235,270 in national bank-notes. The State bank-notes amounted to $142,919,638 on July 1, 1865, three months after Appomattox, but had been slightly surpassed by the national bank-notes, which now amounted to $146,137,860. The arrival of the date for the enforcement of the ten per cent. tax, a year later, found $19,996,163 in circulation in State bank-notes and $276,012,713 in national bank-notes. The State bank-notes dwindled to $4,484,112 a year later, and their last appearance in the Treasury reports was on July 1, 1876, when the amount was stated at $1,047,335. The Act levying the ten per cent. tax was several times revised and was extended in the Act of March 26, 1867, to every national or State banker paying out the notes of any town, city, or municipal corporation after May 1, 1867.[1] The law was finally re-enacted by sections 19, 20, and 21 of the Act of February 8, 1875, so as to apply the ten per cent. tax to persons, firms, or corporations

[1] The Attorney General, on November 21, 1893, in an opinion regarding a clearing house certificate of deposit, declared that the paper was "not within the meaning of the statute," and cited the rule of law that "If there is any doubt as to the meaning of the statute imposing this tax the doubt must be resolved in favor of exemption."—*Official Opinions of the Attorneys General*, XX., 682. The Solicitor of the Treasury gave an opinion on September 28, 1894, in regard to a proposed issue of county bonds of small denominations for use as a local currency, "that no statute of the United States prohibits the issue of county bonds in any denomination." He also observed "that the word 'county' is not enumerated among the corporations, banking associations, etc., mentioned in the statute; nor can the word 'notes' be held to include county bonds." Both these opinions referred to the similar language of the Act of February 8, 1875, then in force.

paying out their own notes or those of any person, firm, or corporation other than a national banking association.[1]

Several of the States passed laws to aid the State banks in organizing under the national system and many of them made the change during the years 1864 and 1865. The number of banks organized for the year ending October 31, 1864, was 453 with an aggregate capital of $79,366,950, and the number organized for the year ending October 31, 1865, was 1014 with an aggregate capital of $242,542,982. This was the year during which the impending levy of the ten per cent. tax drove nearly all banks desiring to continue their circulation into the new system. The number of organizations for the year ending October 31, 1866, was only 62 and for the next year only 10. The reorganization was accomplished with little friction and without arresting the ordinary business of the banks. The stocks of many of them increased in value and Comptroller McCulloch declared in 1864 that he knew "of no instance in which their real market value had been injuriously affected." Congress gave a preference by an Act of March 3, 1865, to State banks not having over $75,000 of capital in entering the national system, but, in view of the ten per cent. tax on their notes, it was a rather humorous observation which was made by Comptroller Clarke, who succeeded Mr. McCulloch, that "nearly all of the State banks voluntarily changed."

The original limit imposed on the national bank circulation was $300,000,000, and it was provided that $150,000,000 should be apportioned to banks in the States and Territories according to population and the remainder at the discretion of the Secretary of the Treasury, with due regard to existing banking capital, resources, and business. Some conflict

[1] These sections refer in every case to "notes" or "circulating notes," and Mr. Edward Atkinson of Boston has expressed the conviction that they do not impose any tax upon certificates of deposit given by national, State, or private bankers to their depositors, even though such certificates might be printed for even amounts and used for general circulation.—*Journal of Commerce and Commercial Bulletin*, Monday, July 29, 1895.

resulted between this provision and that giving preference to the State banks, and the Comptroller permitted the organization of the latter without limit. No stable State banks existed in some of the Western States, so that their share of banking capital was reduced to a minimum, and the difficulty was increased with the restoration of the Southern States to the Union. The Act of July 12, 1870, therefore, authorized an increase of $54,000,000 in the bank-note circulation, to be apportioned to banks "in those States and Territories having less than their proportion," and a new apportionment was directed to be made as soon as practicable, based upon the census of 1870. Provision was also made for withdrawing $25,000,000 of circulation from banks in States having an excess.

The withdrawal of circulation was found to be difficult, because the notes did not reach the banks or the Treasury for redemption. It was only for the interest of the stockholders of new banks to compel redemption, by paying a premium to brokers to sort out notes subject to withdrawal and send them to the Treasury. The inflation bill vetoed by President Grant in 1874 contained a provision for adding $46,000,000 to the bank-note circulation. Congress took a new tack after the veto, and provided for the withdrawal of $55,000,000 of circulation from States having an excess and its issue in States having a deficiency. This Act,—that of June 20, 1874,—was the first to provide for the voluntary retirement of circulation by the deposit of lawful money with the United States Treasurer and the return of the bonds to the bank. The panic of 1873 and the redundancy of currency which followed, led to the voluntary retirement of circulation, so that no requisitions upon the Eastern banks were required to execute the Act of 1874. The Act for the resumption of specie payments, approved January 14, 1875, wiped out any specific limitation upon the amount of national bank-notes and declared that "each existing banking association may increase its circulating notes in accordance with existing law without respect to said aggregate limit; and the provisions of law for the withdrawal and

re-distribution of national bank currency among the several States and Territories are hereby repealed."

The national banks bore an honorable part in bringing about the resumption of specie payments. A few bankers who had extended their speculations beyond legitimate limits undoubtedly desired to see the *régime* of irredeemable paper perpetuated, but the majority were earnestly in favor of return to a specie basis. Secretary McCulloch strongly urged resumption in his first annual report in 1865 and was authorized by the Act of April 12, 1866, to receive legal tender notes for bonds and cancel the notes to an amount not exceeding $10,000,000 in the first six months and $4,000,000 in any one month thereafter. The maximum price of gold, which had been 233.75 in 1865, was 167.75 in 1866 and 145.625 in 1867. Secretary McCulloch reduced the outstanding legal tenders from $422,424,007 on March 31, 1866, to $356,000,000 in February, 1868. The fear of contraction, stimulated by the reaction from the fever of the war speculation, seized upon Congress and the further retirement of legal tender notes was forbidden by the Act of February 3, 1868.

The Resumption Act was the outcome of a caucus committee appointed by the Republicans in December, 1874, to frame a measure upon which the party could unite. The previous session had witnessed the passage of the inflation bill, increasing the limit of legal tender issues to $400,000,000 and authorizing an addition of $46,000,000 to the bank-note circulation, to be distributed to banks in the West and South. The bill was vetoed by President Grant and the inflation fever was checked. The Resumption Act was hurried through Congress within six weeks after the beginning of the session and was intentionally left in clumsy and ambiguous shape in order to hold votes. Senator Schurz of Missouri repeatedly inquired of Senator Sherman, who had the bill in charge, whether the legal tender notes redeemed in coin, as proposed by the bill, were to be retired and cancelled. Mr. Sherman refused to give a definite reply and Mr. Schurz voted with the Democratic Senators against

the bill.[1] Its redeeming feature was the provision for the resumption of specie payments at the New York sub-Treasury on January 1, 1879, and the issue of bonds to obtain the necessary coin.

The success of specie resumption depended largely upon the action of the banks. They held more than $125,000,000 in legal tender notes, of which nearly one-third was in New York City. A run upon the sub-Treasury for gold by means of these notes would have quickly compelled a new suspension of specie payments. The subject of resumption was discussed by the banks and a committee was appointed to confer with Secretary Sherman and agree upon a common course of action to sustain the public credit. The Assistant Treasurer at New York was invited to become a member of the Clearing House and balances between the banks and the Treasury were proposed to be settled through the Clearing House. The banks voluntarily decided to decline receiving gold as a special deposit, to abolish special exchanges of gold checks at the Clearing House, and to receive and pay balances without discrimination between gold and legal tender notes. This action dissipated all serious fear of the success of resumption, and on December 17, 1878, gold sold at par in the gold room of the New York Stock Exchange. The banks, in the language of Mr. Bolles, at the beginning of the war "parted with their gold to aid the government, and now, when resumption was accomplished, they were content to take whatever it desired to give."[2]

It was the policy of the Resumption Act to reduce the volume of United States legal tender paper at the rate of 80 per cent. of the new national bank-notes issued and to continue redemption until the legal tenders should be reduced to $300,000,000. The expectation that the bank currency would rapidly expand to fill the void left by the retirement of the legal tenders was not fulfilled. The circulation

[1] Mr. Sherman, when Secretary of the Treasury, resolved this doubt in his annual report for 1877, in favor of re-issuing the notes, but his opinion was soon deprived of practical importance by the resolution of May 31, 1878, forbidding the further retirement of legal tender notes.

[2] *Financial History of the United States*, III., 301.

secured by bonds reached a maximum of $350,692,966 on December 1, 1873, and fell rapidly from that time until November 1, 1876, when the amount was $301,658,372.[1] The price of bonds as well as the redundancy of currency was beginning to exercise the restraining influence on bank-note circulation which in subsequent years forced it within a narrow compass. The contraction of the bank-note circulation and the retirement of government currency alarmed the advocates of an ample money supply and led to the resolution of May 31, 1878, providing for a second time that it should not be lawful "for the Secretary of the Treasury or other officers under him to cancel or retire any more of the United States legal tender notes." The volume of legal tenders in circulation on the day the Act became law was $346,681,016, and has remained rigid at this amount since that date, except for the addition of the Treasury notes issued under the Sherman law and the temporary retention of notes in the Treasury.

There was a slight tendency to increase bank-note circulation for a time after the revival of business in 1880,[2] but the increase was sharply arrested in the winter of 1881 by the passage of a bill requiring the banks to deposit a new issue

[1] The aggregate circulation on the earlier of these dates was $352,621,762 and on the later date $323,241,308. The difference between "secured" and actual circulation is made up by deposits of lawful money with the United States Treasurer for the redemption and cancellation of notes still outstanding, for which the bonded security has been withdrawn by the banks. This "lawful money" fund is reduced as fast as the notes are redeemed from it and retired, but the withdrawal of bonds was so rapid that the amount ran as high as $107,588,447 on July 1, 1887. The fund stood at $54,207,975 when the Act of July 14, 1890, (Section 6) directed that it "be covered into the Treasury as a miscellaneous receipt" and that redemptions be made thereafter from the general cash. The notes outstanding redeemable in lawful money on December 31, 1895, were $23,011,661.

[2] One of the causes of the decline in secured circulation, as the date approached for the resumption of specie payments, was the fact that the price of the bonds was falling in currency in order to accommodate itself to the gold basis. This made it profitable to sell before the premium disappeared, as the currency obtained for the bonds was appreciating in value as it approached parity with gold.

of three per cent. refunding bonds as security for circulating notes. This limitation on the class of bonds was accompanied by a drastic provision repealing the authority to reduce circulation and withdraw bonds. The banks generally preferred to retain the existing bonds, paying higher rates of interest, even with the loss of circulation, than to submit to such a measure, and 141 banks hastened to deposit $18,764,434 in lawful money for the retirement of their notes and the withdrawal of their bonds in anticipation of the enactment of the bill. The measure was vetoed by President Hayes, but the result upon the secured circulation was to reduce it from $322,654,721 on February 1, 1881, to $305,587,202 on March 1, 1881. Many of the bonds were deposited again after the adjournment of Congress and the circulation increased to $332,398,922 on January 1, 1882. A gradual decline, whose results may be observed in the following table, marked the history of the secured circulation from 1882 to 1892:

JANUARY 1ST.	AUTHORIZED CAPITAL STOCK.	CIRCULATION SECURED BY BONDS.	TOTAL NOTES OUTSTANDING.
1873	$487,781,551	$344,582,812	$347,066,898
1874	499,003,401	348,624,953	350,848,236
1875	503,347,901	342,333,837	354,128,250
1876	511,155,865	324,484,539	346,479,756
1877	501,392,171	302,020,242	321,595,606
1878	485,557,771	309,890,415	321,672,505
1879	471,609,396	313,218,189	323,791,674
1880	461,557,515	328,773,639	342,387,336
1881	467,039,084	322,832,101	344,355,203
1882	470,018,135	332,398,922	362,421,988
1883	492,076,635	322,386,120	362,651,169
1884	518,031,135	310,953,321	350,482,828
1885	529,910,165	285,496,055	329,158,623
1886	534,378,265	274,466,748	317,443,454
1887	555,865,165	205,316,106	296,771,981
1888	584,726,915	165,205,724	268,398,878
1889	598,239,065	146,372,588	233,660,027
1890	623,791,365	127,742,440	197,230,405
1891	665,267,865	125,660,361	177,287,846
1892	685,762,265	140,084,203	173,078,585
1893	695,148,665	150,526,651	174,404,424
1894	693,353,165	185,194,522	208,538,844
1895	670,906,365	176,667,466	206,513,653
1896	664,076,915	190,616,160	213,627,821

It is obvious that a currency system whose permanent circulation was reduced to $125,000,000 for a population of 63,000,000, had ceased to serve one of the chief purposes for which it was created. The causes are to be found in the rapid payment of the national debt, which reduced the possible basis for circulation; the high price of bonds, which reduced the profit on circulation; and the steady stream of silver money which was pumped into the monetary system under the laws of 1878 and 1890, crowding out other forms of currency. Hostility to the national banks, though frequently expressed in the southern and western parts of the country, was a result rather than a cause of their shrinking circulation. There was filibustering in Congress against the bill to extend their charters, but the fact that their discounts and deposits remained unshaken is the best proof that the business community never seriously doubted that the system would survive. The original law gave the banks corporate powers for twenty years and the new bill proposed their continuance for another twenty years. Mr. Crapo, of Massachusetts, who was in charge of the bill in the House, failed twice to secure consideration, because under the rules it required a two-thirds vote, but he obtained the necessary votes on May 1, 1882, and the bill passed the House on May 17th, by a vote of 125 to 67. It passed the Senate with amendments on June 22d and became law on July 12th.

The essential cause of diminishing circulation was financial rather than political and was chiefly found in the growing wealth and credit of the country. The bonded debt of the United States shrivelled from $1,639,567,750 on June 30, 1881, to $610,529,120 on June 30, 1891, and the result was the wiping out of two large bond issues and almost the extinction of a third. The national banks, which had $360,488,400 in bonds on deposit to secure circulation at the earlier date, had only $142,508,900 on deposit at the later date, although the proportion to the whole remained almost exactly the same. The price of bonds, as secure gold investments, rose to such a point that their investment value fell far below three per cent., and their price was enhanced by

the large purchases by the government in advance of maturity made necessary by the enormous surplus accumulating in the Treasury. These purchases of bonds at a premium, exclusive of redemptions at par at maturity, were $51,464,300 for the fiscal year 1888; $120,674,450 for the fiscal year 1889; $104,546,750 for the fiscal year 1890; and $45,175,200 for the fiscal year 1891, after which purchases ceased. The highest average price paid by the government for four per cent. bonds was 128.66 in 1889, when $38,106,400 were purchased. The lowest average price was 124.23 in 1891, two years nearer maturity, when $42,641,250 were purchased.[1] These bonds remained, after the maturity of the four and a half per cent. loan in 1891, the chief source of security for national bank-note circulation, and their price, including the premium, could be more profitably loaned in many cases in the open market than by obtaining ninety per cent. of the par value of the bonds in circulating notes.[2] The clamor of demagogues against the "double interest" derived from the circulating notes and the interest on the bonds was less eloquent of the facts than the steady withdrawal of bonds because circulation had ceased to be profitable. The increase in circulation since 1891 has been due to the fall in the premium on the bonds as they have approached maturity and to special causes, referred to elsewhere, connected with the crisis of 1893 and the bond issues of 1894, 1895 and 1896.

The effect of the increase of the silver circulation under the Bland-Allison Act of 1878 and the Sherman compromise Act of 1890, in driving bank-notes out of existence can only be roughly estimated. It was probably much less potent

[1] These figures are taken from a communication of Secretary Carlisle to the Senate, Sept. 26, 1893, in response to a resolution of that body.—Sen. Ex. Doc. 18, Fifty-third Congress, 1st Sess.

[2] The recommendation was several times made by the Comptroller of the Currency, and embodied in bills introduced in Congress, after the resumption of specie payments, that the banks be authorized to issue circulation to the face value of the bonds deposited as security, instead of ninety per cent. of that value; but no such measure ever became law.

than the rise in the price of bonds, and had more effect in expelling gold than bank-notes from the circulation. The Bland Act, which was passed over the veto of President Hayes on February 28, 1878, authorized the Secretary of the Treasury to purchase not less than $2,000,000 nor more than $4,000,000 worth of silver monthly and coin it into standard silver dollars of 412½ grains each, nine-tenths fine. Every Secretary of the Treasury confined his purchases closely to the minimum and the aggregate purchases, until the act was superseded by the Act of 1890, were 291,272,019 fine ounces, at a cost of $308,279,261, which was coined into 378,166,793 standard silver dollars. The Act of 1890, which was approved by President Harrison on July 14th, took effect thirty days after its passage and provided for the monthly purchase by the Secretary of the Treasury of four and a half million ounces of silver bullion at the market price, and the issue of Treasury notes "redeemable on demand in coin," in payment for the bullion. The purchases under this act were 168,674,682 fine ounces of silver at a cost of $155,931,002. These two measures added to the circulation, therefore, $534,097,795 in currency secured by silver, although the notes issued under the Act of 1890 are redeemed in gold, and have been treated in most respects by the government upon the same footing as other United States legal tender notes. The provision of the Act of 1890 authorizing purchases of silver bullion was repealed on November 1, 1893, but the portion repealing the Act of 1878 was left in force, so that all purchases of silver ceased on that date. The currency in circulation outside the Treasury on that date was $1,718,544,682, of which $498,121,679 was stated to be in gold coin, $78,889,309 in gold certificates, $472,710,610 in the two forms of legal tender notes, $384,443,050 in silver and silver certificates, and only $197,745,227 in national bank-notes. The bank-notes formed less than one-eighth of the circulation, and the $11,566,766 in the Treasury formed a much smaller proportion of the money there held.

The redemption system established by the national banking act of June 3, 1864, provided for redemption in lawful

money of the United States at the office of the issuing bank and at some designated bank in a reserve city. The banks of the reserve cities were required to have a redemption agent in New York. The fact that the notes could be redeemed only in government paper money, which was of no greater value than the notes, prevented any general movement for redemption and gradually filled the channels of circulation with worn and mutilated currency. The notes of the banks distant from the reserve cities drifted only slowly into the redemption agencies and they were rarely sent at the expense of the bank which received them to the issuing bank for redemption. Several propositions were made to enforce prompt redemption, but nothing was enacted into law until 1874. The banks were required by an act of that year to pay into the Treasury of the United States a fund equal to five per cent. of their circulation, which was to be constantly kept good, for the redemption of mutilated notes. Mutilated notes received by any of the banks or the sub-Treasuries were to be sent to Washington for redemption and the expenses of the entire redemption agency and of the transportation of the notes were charged against the banks and then taken from the five per cent. fund.

Redemptions under the new system have been sufficiently rapid to withdraw notes which are badly worn, but have not been rapid enough to give elasticity to the volume of the currency. Where redemptions under the Suffolk system, with a circulation of $40,000,000, were $400,000,000 per year, redemptions under the national system have never been higher than $242,885,375 with a maximum circulation of $355,448,578, and have averaged less in recent years than $100,000,000 with a circulation in the neighborhood of $200,000,000. The aggregate redemptions of national bank-notes for the twenty-one years ending June 30, 1895, were $2,435,706,768. The annual redemptions under the Suffolk system, therefore, were ten times the circulation, while those under the national system have been less than one-half of the circulation. The economy of management was greatly in favor of the Suffolk system. The charges for twenty-one

years under the national system were $3,660,110, or an average of about $175,000 per year. The charge has been reduced in recent years, in more rapid proportion than the reduction of the circulation, so that the rate is now below this average. The cost, however, under the Suffolk system was about ten cents per $1000, while under the national system the lowest rate (in 1895) was about ninety-two cents per $1000. This does not include the costs of transportation, which are charged against the banks.

The original banking act authorized the Comptroller of the Currency to appoint suitable persons to make examinations of the affairs of the banks at such times as the Comptroller thought proper and to make a full report to him. These officials were to be paid by the banks, but the expense was a charge levied by the Comptroller, and fixed by him, so that it did not make the examiner in any way subservient to the bank. Examinations were originally made on an average of about once a year, and other information was obtained by the Comptroller from four reports of condition required during the year, not at the end of each quarter, but at such dates as he saw fit to designate. The frequency of these reports was increased in 1870 to five per year, and the examinations were gradually made more severe as defects in the existing system were disclosed. The same person made all the examinations within a given district until the spring of 1893, when Comptroller Eckels adopted the plan of shifting the examiners of adjoining districts from time to time and of making two examinations during the year instead of one. The original purpose of the system of examination was the protection of the government and of the stockholders against palpable fraud, and was not intended to remit in any degree the vigilance of the directors of the banks. The public came by degrees to look more and more to the government examinations for the assurance of the soundness of the banks, and the system has become one of the most important and characteristic features of American banking.

The rapid expansion of the banking business of the country is indicated in the following table, showing the number

of national banks, with their discounts and individual deposits at dates near the beginning of each year from the organization of the system to the present time : [1]

YEAR.	NO. OF BANKS.	LOANS AND DISCOUNTS.	INDIVIDUAL DEPOSITS.
1864	139	$ 10,666,095	$ 19,450,492
1865	638	166,448,718	183,479,636
1866	1,582	500,650,109	522,507,829
1867	1,648	608,771,799	558,699,768
1868	1,642	616,603,479	534,704,709
1869	1,628	644,945,039	568,530,934
1870	1,615	688,875,203	546,236,881
1871	1,648	725,515,538	507,368,618
1872	1,790	818,996,311	596,586,487
1873	1,940	885,653,449	598,114,679
1874	1,976	856,816,555	540,510,602
1875	2,027	955,862,580	682,846,607
1876	2,086	962,571,807	618,517,245
1877	2,082	929,066,408	619,350,223
1878	2,074	881,856,744	604,512,514
1879	2,051	823,906,765	643,337,745
1880	2,052	933,543,661	755,459,966
1881	2,095	1,071,356,141	1,006,452,852
1882	2,164	1,169,177,557	1,102,679,163
1883	2,308	1,230,456,213	1,066,901,719
1884	2,529	1,307,491,250	1,106,453,008
1885	2,664	1,234,202,226	987,649,055
1886	2,732	1,343,517,559	1,111,429,914
1887	2,875	1,470,157,681	1,169,716,413
1888	3,070	1,583,941,484	1,235,757,941
1889	3,150	1,676,554,863	1,331,265,617
1890	3,326	1,811,686,891	1,436,402,685
1891	3,573	1,932,393,206	1,485,095,855
1892	3,692	2,001,032,625	1,602,052,766
1893	3,784	2,166,615,720	1,764,456,177
1894	3,787	1,871,574,769	1,539,399,795
1895	3,737	1,974,623,974	1,695,489,346
1896	3,706	2,020,961,792	1,720,550,241

[1] These figures are taken from the reports of condition called for by the Comptroller and the dates are those of the reports nearest to the first day of the year for which they are given. Reports were called for during the early days of January up to 1870, since which time they have usually been called for late in December or not until late in February. The reports for December of the preceding year are taken in these cases, as representing more nearly the condition on January 1st, than those of several weeks later. The earliest of these December reports was December 16th in 1871, but most of them were for the last two or three days of the month. The growth of deposits in recent years in State and savings banks is shown in Chapter xxiii.

The suspension of purchases of silver bullion and the issue of circulating notes under the Sherman law left the United States, in view of the limitations of the national bank-note circulation, without any means of materially increasing their currency. The importance of a currency system more adapted to commercial needs, and capable of greater expansion in the South and West, was under discussion among Democratic leaders for several years before the panic of 1893 and began to assume definite shape during the discussion on the repeal of the Sherman law. It was believed by many that the clamor for the free coinage of silver was largely stimulated by the lack of an elastic circulating medium in the newer sections of the country and that this clamor would end, except in the small silver-producing States, if such a medium were provided. The democratic national platform, adopted at Chicago, June 21, 1892, contained the declaration, "We recommend that the prohibitory ten per cent. tax on State bank issues be repealed." This declaration was not interpreted by conservative members of the party in the North as a declaration for unconditional repeal, and when that question was submitted to the House of Representatives on June 6, 1894, it was rejected by a vote of 102 in the affirmative and 172 in the negative, the negative vote including 74 Democrats, nearly all from the Northern States.

The division of opinion existing in the country on the banking problem was indicated by the divisions in the House Committee on Banking in the long session of the Fifty-third Congress in the spring and summer of 1894. The Chairman of the Committee, Mr. Springer of Illinois, declared himself at an early date opposed to the unconditional repeal of the tax on the circulation of State banks, and when a vote was taken in committee the majority were found to agree with him. They never reached an agreement during the long session of Congress, however, upon any affirmative measure. The Northern Democrats who appreciated the importance of currency reform presented a number of bills proposing a banking currency. Mr. John

De Witt Warner of New York was the most active upon this side and proposed the remission of the tax on both State and national banks when they conformed to certain prescribed conditions. These conditions involved making the notes the first lien upon the assets, adequate provision for redemption of notes, a paid-up capital of not less than $50,000, the limitation of the circulation to 75 per cent. of the capital, and the payment of an assessment for a guarantee fund for the redemption of the notes. A plan like this was the basis of most of the measures for a banking currency which were offered by the Northern members, but most of the Southern Democrats felt bound to put themselves on record in favor of unconditional repeal of the ten per cent. tax in order to prove their sincerity to their constituents. The result was the failure to agree upon any definite measure.

The necessity of some new banking legislation was strongly urged upon President Cleveland by Representative Oates of Alabama and other prominent members of Congress while the repeal of the Sherman law and the tariff bill were pending. The President spoke in an encouraging manner of the necessity of currency reform, but he refrained from complicating the other issues before Congress by any specific recommendations until the meeting of the short session on December 3, 1894. The dissatisfaction with the system of note issues authorized by the national banking law and the belief that a different system must be substituted had been steadily growing, and the adoption of a new system was advocated by many of the most influential bankers of New York and Boston. A convention of bankers at Baltimore on October 18, 1894, declared in favor of permitting the issue of circulating notes by existing national banks up to the amount of 50 per cent. of their paid-up capital, secured by general assets and by a guarantee fund deposited by the banks with the United States Treasurer. This guarantee fund was to be paid into the Treasury to the amount of two per cent. of the circulation of the banks the first year and thereafter at the rate of one-half of one per cent. per year until the entire amount was five per cent. of the outstanding circula-

tion, and the government was to have a first lien upon all the assets of a failed bank, in order to ensure the redemption of the notes to the holders. An emergency circulation was also authorized to the amount of 25 per cent. of the capital, subject to a heavy tax upon the average amount outstanding for the year. The exact rate of this "heavy tax" was not specified, but its purpose was to compel the retirement of the "emergency circulation" when the demand for money was not acute enough to justify a high rate of interest.[1]

Manifestations like these paved the way for the formal presentation of the subject to Congress in the message of President Cleveland and the annual report of Secretary Carlisle. The President urged in emphatic language the necessity of radical currency reform, but he left the exposition of the details to his minister of finance. The need of action was emphasized by the large exports of gold and the continuous pressure of the redundant paper currency of the government upon the dwindling gold reserve. This redundancy of the legal tender currency had stimulated a powerful demand for its retirement, which was ably supported in New York by Mr. William Dodsworth of the *Journal of Commerce and Commercial Bulletin* and in Boston by Mr. Charles C. Jackson.[2] Mr. Carlisle was not a believer in legal tender paper and would probably have been glad to recommend its absolute retirement by means of a loan, but out of deference to possible opposition to such radical action he contented himself with proposing the locking up of the legal tender notes as security for the proposed new bank-note cir-

[1] See the interesting testimony of Mr. Horace White before House Committee on Banking, Dec. 11, 1894, House Report 1508, 3d. Sess., Fifty-third Congress, 80–100. Mr. White presented a bill, on his own responsibility, making the tax on emergency circulation four per cent., in addition to the other taxes required on circulation in the first year.

[2] The Democratic State Convention of Massachusetts, under the influence of John E. Russell, Henry C. Thacher, and George Fred. Williams, adopted a resolution demanding "that the government shall, with the development of a banking system adequate to the demands of trade, retire as rapidly as possible all its legal tender paper money." The demand was reiterated in the Democratic State platform of 1895.

culation, in much the same way in which the Canadian banks are required to hold forty per cent. of their circulation in Dominion notes. Mr. Carlisle's propositions for currency reform may be summarized in their important features as follows :

1. Repeal all laws requiring, or authorizing, the deposit of United States bonds as security for circulation.

2. Permit national banks to issue notes to an amount not exceeding seventy-five per centum of their paid-up and unimpaired capital, but require each bank before receiving notes to deposit a guarantee fund consisting of United States legal tender notes, including Treasury notes of 1890, to the amount of thirty per centum upon the circulating notes applied for. . . .

3. Retain the provision of the law making stockholders individually liable, and provide that the circulating notes shall constitute a first lien upon all assets of the bank.

4. No national bank-note to be of less denomination than ten dollars, and all notes of the same denomination to be uniform in design ; but banks desiring to redeem their notes in gold may have them made payable in that coin.

5. Require each national banking association to redeem its notes at its own office, or at its own office and at agencies to be designated by it.

6. Provide a safety fund by taxation upon the banks for the immediate redemption of the circulating notes of failed banks and require the legal tender guarantee fund of a failed bank to be paid into the safety fund. The safety fund may be invested in outstanding United States bonds having the longest time to run, the bonds and the interest upon them to be held as part of the fund and sold when necessary to redeem notes of failed banks.

7. Repeal all provisions of the law requiring banks to keep a reserve on account of deposits.

8. The Secretary of the Treasury may, in his discretion, use any surplus revenue of the United States in the redemption and retirement of United States legal tender notes, but such redemptions shall not in the aggregate exceed an

amount equal to seventy per cent. of the additional circulation taken out by national and State banks.

9. Suspend the ten per cent. tax on the circulation of banks duly organized under the laws of any State, transacting no other than a banking business, and complying with the second and third provisions just named and promptly redeeming their notes at the principal offices and branches. The guarantee fund in United States legal tender notes was to be permitted to be kept by the State banks in their own custody, but must at all times equal thirty per cent. of the outstanding circulation.[1]

These propositions, embodying the essential principles of an elastic banking currency, were cordially approved by many bankers and financial journals, but the presentation of a bill to carry them out, prepared by Mr. Carlisle, led to an acrimonious discussion in which party politics were largely involved, and in which the merits of the general scope of the plan were so much obscured by criticism of details that many bankers who were not opposed to a banking currency became hostile to any immediate legislation on the subject. Mr. Carlisle himself appeared before the banking committee in support of his bill and the other witnesses who appeared for or against the measure included some of the most eminent bankers of the country. The Committee on Banking closed the hearings on December 15, 1894, and voted on that day to report Mr. Carlisle's bill to the House, with some amendments. The Republican members did not concur in reporting the bill or in closing the hearings so promptly. Several of the Democrats also were opposed to details of the measure, but were willing to have it reported for consideration. It was contended by Mr. Sperry of Connecticut and other members that the bill did not meet the most pressing financial necessity of the hour, which was the retirement of legal tender notes and provision for the pro-

[1] Most of these propositions are quoted verbatim from the annual report of the Secretary of the Treasury to Congress (pp. lxxvi–viii), but it has been necessary to omit subsidiary features and details which are the natural complement of the principles laid down.

tection of the gold reserve. Mr. Sperry and Mr. Warner of New York united in a request, at the meeting of democratic members of the committee on December 20th, that provision be made for the continuance of the existing system of note circulation, in order not to compel too sudden a transition to the new system, and that the provision imposing unlimited liability upon the banks for the redemption of the notes of failed banks be modified. Both of these changes were accepted by the majority.

Chairman Springer of the Committee on Banking introduced a substitute for the original bill on December 21st, embodying the various amendments which had the consent of Secretary Carlisle. A caucus of democratic members of the House was held on January 7, 1895, and it was voted, 81 to 59, to proceed with the consideration of the bill in the House. This vote was not encouraging to the advocates of a banking currency, because it was known that the Republicans would oppose the bill and that they would constitute, with the minority of Democratic members, a majority of the House. It was found that the extreme silver men would not support the bill and they cast a vote of 54 against 64 in the caucus for a substitute measure, offered by Mr. Terry of Arkansas, to authorize the Treasury to issue notes upon silver bullion deposited by the various States. Some of the more moderate silver men were willing to abide by the decision of the majority of the party, but their votes were offset by those of Eastern members who did not consider the committee bill sufficiently guarded in its provisions. The belief that the bill could not pass the House was verified when the vote was taken on January 9th on the question of consideration. The affirmative vote was 122 and the negative vote was 129. This margin might have been overcome if all those voting for consideration could have been trusted to support the bill, but it was well known that a considerable number of them would not vote for the measure on its passage. Some further efforts were made among members of Congress to secure an agreement on a banking measure, but they were not successful. The subject of maintaining

the government gold reserve became more pressing than that of banking reform, during the brief period remaining before the termination of the session of Congress on March 4, 1895, and was the subject of the bills subsequently reported by the Banking Committee.

The Fifty-fourth Congress, which met on December 2, 1895, contained majorities politically hostile to the administration of President Cleveland. This fact and the continued danger of the gold reserve led the President in his message, and the Secretary in his annual report, to make the subject of the maintenance of the gold reserve paramount to suggestions of radical changes in the banking laws. Secretary Carlisle simply renewed the recommendations, repeatedly made in former years by the Comptroller of the Currency, that the banks be given greater freedom of note issue by permission to issue circulation to the par value of the bonds deposited as security, and that the tax on circulation be reduced from one-half to one-quarter of one per cent. annually. He pointed out that until 1883 there was a tax upon the capital and deposits of national banks, as well as a tax upon their circulation, and that from all these sources the government received up to the close of the fiscal year 1895 the sum of $146,902,962. From the tax on circulation alone the receipts amounted to $78,107,006, while the total estimated expenses of supervision, including salaries of officials, had been only $15,636,976. The average annual cost of supervision, declared the Secretary, "has been $473,848, while a tax of one-fourth of one per cent. on the average annual circulation would have yielded $680,294." The Secretary also stated that "The gain to the government on account of national bank-notes lost or destroyed, and which are consequently, never presented for redemption, is estimated to be two-fifths of one per cent. upon the total amount issued, and has, according to this estimate, amounted to the sum of $2,805,715." [1]

[1] The amount of paper currency lost or destroyed and never presented for redemption is much smaller than is popularly believed. No exact figures have ever been obtained, because notes of the oldest

Two important changes suggested by Secretary Carlisle were the transfer of the current redemption of national bank-notes from the United States Treasury to agencies established by the banks and designated by the Comptroller of the Currency, as was the case prior to the Act of June 20, 1874, and that national banks be permitted to establish branches for the transaction of all kinds of business except the issue of notes. The Secretary suggested as an alternative plan, in case the redemption agency at Washington was continued, that the banks be required to maintain their five per cent. redemption fund in gold coin and to deposit gold coin for the withdrawal of bonds whenever circulation was to be permanently surrendered or reduced. This suggestion was a part of the policy of withdrawing the legal tender notes of the government recommended by the President and Secretary, and was for the purpose of supplying the Treasury with a proper medium for the redemption of bank-notes after the retirement of the government notes. The establishment

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issues are occasionally received for redemption, and even an approximate estimate can be made only upon issues of many years standing. No calculation based upon such issues has shown a larger average loss, except upon the small fractional currency, than one per cent. and Secretary Carlisle's estimate of two-fifths of one per cent. is probably not too small. The percentage applies, however, to the entire issues rather than to the net amount in circulation at any one time. The entire issues of United States notes up to the close of the fiscal year 1895 were $2,725,981,808, and two-fifths of one per cent. of this amount would be about $10,000,000. The total issues of national bank-notes to October 31, 1895, were $1,906,918,995, and the proportion of estimated loss would be about $7,500,000. This loss, however, will not be realized until all the recent issues have been many years outstanding, which accounts for the variation from the estimate of Mr. Carlisle. One of the proofs of the small percentage of loss upon paper currency is furnished by the old demand notes, of which $60,030,000 were issued and only $54,847, or less than one-tenth of one per cent., were outstanding on June 30, 1895. These notes, however, having been received for customs in common with gold, did not remain so long in circulation as some other forms of paper currency. Of $1 and $2 notes in circulation in Canada on June 3, 1871, less than one per cent. were outstanding in 1894.—Breckenridge, 337.

of branches by the national banks was cordially approved by the President.

Comptroller Eckels followed the President and Secretary of the Treasury in abstaining from recommending a new basis for the issue of bank-notes, but he indicated his belief in the policy of an elastic banking currency in the following terms: [1]

> The advantage accruing to the Government by the substitution of a bank-note for a Treasury-note currency would be immeasurably great. The need of maintaining a gold reserve to meet the recurring demand obligations, now never retired, would, within a reasonable time, be obviated, and, delivered from this vexatious and expensive difficulty, the Treasury Department could return to its legitimate function of collecting the revenues of the Government needful to meet governmental expenses and disbursing the same.
>
> With the relief gained to it through the removal of this burden would come a greater one to the business interests of the individual citizen, whose every operation would no longer be harassed by the uncertainty springing from a fear that either in the present or the future the currency obligations now forced by his Government through the provisions of an inflexible law into the avenues of trade and commerce may be discredited and dishonored. The relegating of note issuing entirely to the banks would give a better guarantee of meeting the varying wants of trade, which is impossible with a legal mandate decreeing an amount of Treasury issues of no greater and no less volume at one season of the year than another, whether or no there be a corresponding increase or lessening of the demand for currency to transact the business in hand.

[1] Comptroller's Report, 1895, 23.

CHAPTER XVI.

THE CANADIAN BANKING SYSTEM.

Its Origin and Growth—Foundation of the Bank of Montreal—The Union of the Canadian Provinces and the Dominion—Banking Reforms in 1870, 1880, and 1890—The Effect upon the Security of Note Issues and the Small Losses by Failure—Recent Suspensions.

THE Canadian banking laws now in force represent an almost steady growth from comparatively crude conditions to a perfected scientific system. Founded originally upon Scotch models, the Canadian banks enjoyed at first the freedom from even the police supervision of the government which naturally arose from the fact that they framed their own charters. Canadian banking was not exempt from the risks and difficulties of the other institutions of a new and growing country, and defects in the security of the note issues and the protection of deposits were gradually remedied as they were disclosed by experience. The development of the Canadian system, however, has been natural and symmetrical and most of the changes in the law have had the approval of the leading bankers. Attempts have been several times made to substitute a government currency or a specially secured circulation for the elastic medium provided by the banks, but these attempts have not been sufficiently successful to destroy the essential advantages of the Canadian banking system. They have resulted in putting a considerable volume of government paper alongside the bank-note currency and in requiring a certain percentage of this paper to be held by the banks in

their cash reserves, but they have not supplanted the bank-note currency and are not likely to be permitted to, unless the necessities of the government in time of war should become paramount to the commercial interests of the country.

The history of Canada is that of several separate provinces before the union in 1841. The movement for better banking facilities began independently, but almost simultaneously in each province early in the present century. The scarcity of specie or of any other circulating medium in Lower Canada was partially supplied by the "Army bills" issued by the government during the war with the United States and it was not until 1817 that a banking company was formed.[1] Previous attempts to found a bank had been addressed to the local legislature of Lower Canada, but on June 23, 1817, a meeting was held at Montreal at which an association was formed with a capital stock of £250,000. An office was opened in August under the title of the Bank of Montreal, without waiting for legal authority, and what afterwards became the strongest institution of the Dominion was thus established. The bank was simply a private partnership, with unlimited liability of the shareholders, and continued so until the passage of a charter by the legislature on March 17, 1821, which was approved by the royal government and proclaimed on July 22, 1822.

Charters for the Quebec Bank and the Bank of Canada, situated at Montreal, were passed at the same session of the legislature and their approval by royal authority was proclaimed on November 30, 1822. The Quebec Bank had been organized in a similar manner to the Bank of Montreal on July 9, 1818, with a capital of £75,000, and the Bank of Canada had been organized on August 25, 1818, with a capital of £200,000. The charter of the Bank of Montreal, whose provisions were followed in the charters of the other two banks, gave the institution corporate powers until June

[1] The Army bills outstanding at the close of the war in March, 1815, were £1,249,996, but they were receivable for public dues and convertible into government bills of exchange on London, and were reduced by May, 1816, to £200,000.

1, 1831, and provided for the choice of thirteen directors, who must be British subjects and holders of at least four shares each. The principle of limited liability was applied to the shareholders, without any obligation beyond the amount of their subscription to the stock, but the directors were to be liable to the stockholders as well as to the holders of bank-notes in case the debts of the corporation should exceed treble the amount of the capital stock actually paid in, exclusive of the deposits. The bank was prohibited from lending on land or mortgage, but might take such property for debt contracted in the course of its legitimate dealings.

The fact that the acts passed by the provincial legislature for the incorporation of these banks were based upon the articles of agreement drawn by the incorporators made the restrictions trifling which were imposed upon the banks. There was no limit upon the volume of note issues except the general liability of the directors for the aggregate indebtedness. There was no prohibition upon loans upon the stock of the bank or upon loans to directors. The fact, however, that each bank was established by a special law afforded some measure of protection against indiscriminate private banking and there was a disposition from the outset to adhere closely to Scotch methods.[1] An indication of this is given by the prompt establishment of branches by the Bank of Montreal at Quebec and by both the Bank of Montreal and the Bank of Canada at Kingston in the upper province. The banks received the notes of their competitors and exchanged them and settled the balances in specie as often as once a week, according to the Scotch system. The Bank of Montreal employed an agent in New York for the negotiation of sterling exchange and all the Canadian banks of importance eventually had an agent or correspondent in the American metropolis.

[1] Mr. R. M. Breckenridge, in his admirable work, *The Canadian Banking System*, published by the American Economic Association, from which many of these facts regarding early Canadian banking are taken, states that among 140 odd charter members of the Bank of Montreal there were at least 90 Scotch names.

The importance of freedom of note issues in developing banking in a new country is indicated by the early returns of the Canadian banks, in spite of the considerable deposits which they were able to obtain. The total deposits of the three banks of the lower province in 1824 were £135,426, while the circulation was £167,498; the deposits in 1825 were £151,637 and the notes in circulation £177,454; the deposits in 1826 were £176,475 and the notes £193,548. The debts due to the banks, which may be assumed to represent chiefly the discounts, were £529,363 in 1824, £585,265 in 1825, and £594,515 in 1826. The debts due the Montreal Bank in the latter year were £371,334; Quebec Bank, £111,523; and Bank of Canada, £111,658. The banks secured the renewal of their charters in 1830 and 1831, until June 1, 1837. The legislation of this time cut off possible note issues by private bankers, by prohibiting notes payable to bearer except when issued by banks incorporated by law in Lower Canada. The total amount of notes in circulation for less than $5 was limited to one-fifth the capital stock of the Bank of Montreal and notes for less than five shillings were prohibited. Similar limitations were imposed upon the Quebec Bank and the power was reserved to the legislature to prohibit or limit entirely the circulation of notes under $5.

The Bank of Canada found its business falling off in 1825 and after gradually reducing its capital stock went into liquidation in 1831, upon the lapse of the charter. The bank did not fail or suspend payments, but adopted a policy of paying uncurrent and underweight coin, which led the Bank of Montreal to refuse its checks and notes and caused the rapid reduction of deposits until it became unprofitable to continue business. A charter was granted to the City Bank of Montreal in 1831, upon the representation of leading merchants that the capital of the existing bank was "altogether inadequate to the circulation of the valuable articles of import and export which its geographic position naturally brings to it," and that the most effectual preventive of the evil of monopoly "is the admission of reasonable

competition, with its counteracting influence." Another Montreal bank began business in 1835 under the title of the *Banque du Peuple* (Bank of the People). The principal partners were Messrs. Viger, De Witt, and Co., who were fully liable for the debts of the bank, while shares were issued to persons having no share in the management and liable only for the amount of their stock, according to the French system of partnership *en commandite*.

The movement for a bank in Upper Canada, now constituting the Province of Ontario, assumed definite shape a trifle earlier than in Lower Canada, but the first charter passed by the provincial legislature did not receive the royal assent within the period provided by the charter to give it validity, so that it became necessary to pass a new charter in 1819. The royal government again delayed action, but the Bank of Upper Canada, situated at Kingston, was finally authorized by proclamation of the royal assent on April 21, 1821, more than a year before such assent was granted for the banks of Lower Canada. The capital of the bank was originally fixed at £200,000, but this was reduced in 1823 to £100,000. The general provisions of the charter were similar to those of the banks of Lower Canada, but notes under five shillings were forbidden from the outset and the charter was to remain in force until June 1, 1848. The government subscribed for 2,000 shares of the capital at a par value of £25,000. A practical monopoly of note issues was conferred upon the bank in 1823 by an act prohibiting banks from carrying on business in the province, which did not redeem their notes in specie within its limits. The development of Upper Canada was somewhat more rapid after the establishment of the bank than before, from a combination of causes, and the capital stock actually paid in increased from £10,640 in 1823 to the full limit of £100,000 in 1830. The debts due by the bank increased from £107,598 on December 15, 1826, to £260,557 on January 1, 1831, and the notes in circulation increased during the same interval from £87,339 to £187,039. The bank encountered only the rivalry of an institution purporting to be the Bank of Upper Canada under

a forfeited character, which soon collapsed, until the incorporation in 1832 of the Commercial Bank of the Midland district. The capital of the new bank was fixed at £100,000. The capital of the Bank of Upper Canada was increased by a like amount at the same session, and the utmost eagerness was shown to purchase the stock. The Commercial Bank within three years sought and obtained power to double its capital stock and an act was passed incorporating the Gore Bank at Hamilton with a capital of £100,000.

The first bank charter in New Brunswick received the royal assent as early as March 25, 1820. The institution was known as the Bank of New Brunswick and was located at St. John, with a capital of £50,000. The shareholders were liable only for the principal of their stock, and debts by the directors, either as principals or indorsers, were limited to one-third of the paid-up capital. The banks were forbidden by an Act of 1838 to issue notes of a less denomination than five shillings. The first bank of issue actually established in Nova Scotia was opened in 1825 at Halifax under the title of the Halifax Banking Company. The Bank of Nova Scotia, which was the first chartered bank, was incorporated by an Act approved March 30, 1832, with an authorized capital of £100,000. The bank was without a chartered competitor for five years and during its first ten years divided profits among the shareholders at the average rate of 8.9 per cent. and increased its capital to £140,000. The issue of bank-notes for less than £5 was prohibited in Nova Scotia in 1834.

The banking system of the Canadian provinces was thus established on a comparatively safe and scientific basis, similar to the Scotch system in the part played by the large incorporated banks and their branches, but without any serious control by law. The history of the next thirty years involves a mania for banking speculation similar to that witnessed in the United States, on the part of the Canadian people, and an effort to apply the rigid limits of the English restriction act on the part of the home government at London. The banking mania seized Upper Canada and resulted

in the creation of several joint stock banks between 1834 and 1837. The creation of such banks without a special charter was brought to a summary end by an Act of 1837, prohibiting the issue of circulating notes, except by banks holding legislative charters, and making such issues a misdemeanor. The banking phrenzy was not checked by this salutary regulation. The House of Assembly had passed a bill in 1833 to enable the Receiver General to issue notes chargeable on the public, and a select committee in 1835 reported in favor of a provincial bank, on the basis of loans guaranteed by the province. These measures alarmed the home government and resulted in a despatch to the Lieutenant Governor August 31, 1836, directing him not to permit any act touching the circulation of promissory notes or the law of legal tender to come into operation in Upper Canada without having first received the royal sanction. This precaution was taken none too early, for bills were passed during the session of 1836–37 increasing the banking capital of the province from £500,000 to £4,500,000 and conferring a power of note issue to the limit of £13,500,000.[1] The Imperial government did not formally disallow these acts, but returned them to the Colonial legislature for more sober consideration. This course was effective and none of the measures were re-enacted.

The union of Upper and Lower Canada was accomplished on February 5, 1841, under the title of the Province of Canada, and banking legislation was henceforth enacted in uniform terms for the entire province. The government of Upper Canada prepared for the union by the sale of the government stock in the Bank of Upper Canada and the separation of the government from official connection with the bank. A scheme was brought forward soon after the union by the Governor General, Lord Sydenham, for a provincial bank of issue under the direct authority of the government. Lord Sydenham was a personal friend of Lord Overstone, the great champion of "the currency principle" in England, and endeavored to engraft upon Canadian

[1] Breckenridge, 77.

finances the separation of the functions of note issue and banking which were imposed upon the Bank of England by the Act of 1844. Lord Sydenham suggested a series of resolutions for a bank, with no other powers than that of issue, with an authorized circulation of £1,000,000 and an excess issued only against coin or bullion. The authorized circulation was to be protected by government securities, of which the interest was to go to pay the expense of managing the bank and any balance to the public Treasury. There was a strong outburst of public feeling against destroying the profits and efficiency of the existing banks and the conservatives, French Canadians, and a few supporters of the party in power, united in committee of the whole on August 31, 1841, in a resolution "that it is inexpedient to take into further consideration during the present session the establishment of a provincial bank of issue, or the issue in any way of a paper currency on the faith of the province."[1]

The committee which considered Lord Sydenham's proposals admitted the propriety of some uniform regulation of the banks, and it had been repeatedly urged in circulars from the home government. These recommendations contemplated the usual safeguards against unsound banking,—limiting the business of the banks to a proper banking business, conducted after the subscription of the capital, and involving forfeiture if specie payments were suspended for sixty days. These restrictions were applied to the three banks of Lower Canada when they sought a renewal of their charters in 1841. Notes under five shillings were prohibited, and notes under one pound were not to exceed one-fifth of the paid-up capital. The various charters were to expire at the end of the first session of Parliament after June or December 1, 1862. Double liability was imposed upon shareholders, and nearly all the provisions for the public security which had prevailed in either Lower or Upper Canada were now applied to the banks of the entire province. The pet theory of the home government, that coin should take the place of small notes, in order to constitute a healthy monetary

[1] Breckenridge, 112.

system, led to considerable correspondence in 1846, pending the approval of a charter passed in that year, but the government finally consented to the retention of the $1 notes.

The mania for "free banking" on securities seized upon the Canadian people towards the middle of the century and resulted in the law of 1850, based upon New York models. William Hamilton Merritt was the author of the new law, and he first brushed away the obstacles by the repeal of the laws prohibiting the circulation of the notes of private bankers. Such note issues were permitted, provided that the banks formed for the purpose deposited Provincial securities with the Receiver-General for not less than $100,000 as a pledge for their notes. One of the objects of this legislation,—to broaden the market for Provincial securities,—was indicated by the provision that these notes were to be exempt from the tax of one per cent. per year imposed on the circulation of the chartered banks, and that the latter might surrender their circulation against their assets, and issue notes upon deposits of securities. The notes, in case of suspension, were to be paid from the proceeds of the securities, and any balance was to be applied, with the other assets, to the settlement of the remaining debts of the bank. The notes were to constitute a preferred claim against other assets in case the proceeds of the securities proved insufficient.

The effort to drive the chartered banks into the secured note system was carried further, in 1851, by a bill granting certain exemptions from taxation to banks which were willing to restrict their circulation to the maximum shown in their last statement and to reduce it in three years to three-fourths of the average for 1849 and 1850. Such banks were permitted to issue additional notes to the amount held in gold or silver coin or bullion, or in debentures issued by the Receiver-General and reckoned at par. They were not required to deposit the debentures, but were required in case of failure to apply them exclusively to the redemption of their notes. The fact that the banks were required to hold the debentures permanently, whether in the custody of the government or in their own vaults, resulted in withdrawing

active capital from commercial banking and offering insufficient inducement to investors of banking capital. Five banks were created under the law, of which two soon disappeared and three were continued under special charters. The Bank of British North America, which operated in all the provinces under a royal charter, apparently obtained the greatest advantages from the secured note system by employing it prudently in connection with its other business. The failure of the "Free Banking Act" was acknowledged as early as 1859, but it was not repealed until the passage of the Provincial Note Act of 1866.

The temptation to use the power of note issue for the benefit of the State assailed the provincial authorities again in 1866, when the government found themselves compelled to raise about $5,000,000 to discharge the floating debt. Mr. A. T. Galt, Minister of Finance, succeeded in carrying a bill, which received the royal assent August 15, 1866, assuming the power of the Province to issue not more than $8,000,000 of notes, payable on demand in specie at Montreal or Toronto and legal tender except at those offices. He did not dare propose the immediate abolition of the bank-note currency, but proposed an indemnity payment by the government of five per cent. per year, on the amount of notes outstanding on April 30, 1866, until the expiration of the charter of any bank which might accept the conditions of the act and withdraw its own circulation before January 1, 1868. Banks willing to accept this offer were relieved from the requirement to invest ten per cent. of their capital in debentures and allowed to exchange them at par for Provincial notes. The Bank of Montreal was the only institution which accepted the new system and gradually substituted Provincial notes for its own issue. This action separated the interests of the Bank of Montreal from those of the other banks and led the former to force the legal tender notes into circulation as rapidly as possible in the settlement of its balances. The Bank of Montreal was able to force the other banks into holding legal tenders by threatening to exact settlements in legal money, which the other banks

were thus compelled to set aside for the purpose. The result was a reduction of the banking resources of the other banks and the complication of the paper currency by the rival circulation of the Provincial notes in competition with bank-notes.

New Brunswick and Nova Scotia were brought within the circle of Canadian banking legislation by the Act of 1867, creating the Dominion of Canada, which conferred exclusive authority in matters connected with currency, coinage, and banking upon the Parliament of the Dominion. The charters of existing banks were extended temporarily to the end of the first session of Parliament after January 1, 1870, and several provisions affecting the Canadian banks were extended to those of New Brunswick and Nova Scotia. The Provincial note issue was consolidated into an issue of Dominion notes and redemption agencies were provided for in the capitals of the four provinces. The banks in existence when the Confederation became a fact on July 1, 1867, were eighteen in Ontario and Quebec, five in Nova Scotia, four in New Brunswick, and one operating in all the provinces under royal charter.

The attempts to create a secured circulation or a government currency were renewed after the creation of the Dominion, and the supporters of the former had the benefit of the example of the United States and the active efforts of Mr. E. H. King, the manager of the Bank of Montreal. A scheme of this sort was taken up by Mr. Rose, the new Minister of Finance, in 1869, and, according to his bill, was to go into effect on July 1, 1871. The banks after that date were to be required to reduce their unsecured circulation twenty per cent. a year until the whole should be retired, and were permitted to issue notes up to the amount of their capital stock actually paid in, bearing on their face the statement that they were secured by the deposit of Dominion securities. These notes were to be legal tender throughout the Dominion, except at the office of the issuing bank, so long as they were redeemed in specie, and were to be protected by a cash reserve amounting to twenty per cent. of the notes

and one-seventh of the deposits subject to call. The notes were to constitute the first charge upon the assets in case of insolvency. The opposition was so strong, and there were so many measures whose success was more important to the ministry, that Mr. Rose announced on June 15th the temporary withdrawal of the plan for the session. Sir Francis Hincks became Minister of Finance before the next session and he abandoned the policy of a specially secured circulation and contented himself with throwing some additional safeguards around the existing bank-note system.

The charters of the banks were extended by the Act of May 12, 1870, for a period of ten years, and the most important changes of the period were then made. The desire for a codification of the banking law led, however, to a more comprehensive act in 1871,[1] which embodied the reforms of 1870 with some minor changes and many amplifications of detail. The banks in 1870 surrendered the right to issue notes below the denomination of $4 and secured in compensation the abolition of the one per cent. tax and the repeal of the requirement to keep one-tenth of their capital in Dominion securities. The government assumed the issue of small notes and the banks were required to hold not less than one-third of their cash reserves in Dominion notes. The severe period of depression through which the Dominion passed between 1874 and 1879, and the several bank failures which occurred, led to further important changes in the banking law when the charters were about to expire in 1880. The bankers themselves came forward with the proposals for reform and were now willing to accept several propositions which they had before rejected. The minimum denomination of notes was changed to $5 and the banks were required to retire the notes for $4 as soon as practicable. The proportion of cash reserve to be held in Dominion notes was increased to forty per cent. The use of the title of "Bank" by a private firm not incorporated under the laws of the Dominion was made a misdemeanor, unless the words "Not

[1] Act of April 14, 1871, "relating to banks and banking," 34 Victoria, c. 5.

Incorporated" were added to the title. This provision was made to prevent the public from mistaking private bankers for those holding charters and was extended in 1890 so that any such expression as "Bank" or "Banking House" was made illegal, whether the words "Not Incorporated" were added or not.

The history of the Canadian banking system between 1880 and the renewal of the bank charters in 1890 was a comparatively uneventful one, but experience of the banking law had suggested a number of reforms which were carefully discussed before the renewal was voted. It was found that the notes of the banks did not remain steadily at par in those parts of the country far removed from the redemption agencies. It was also found that, notwithstanding the ample security for the final payment of the notes of failed banks, they sometimes dropped to a discount when the holders desired to realize upon them at once.[1] The importance of concerted action to secure the reforms desired by the public, without infringing upon the freedom of banking, was keenly felt by the leading banks and they held a meeting in Montreal on January 11, 1890, at which they resolved to request an interview with Mr. Foster, the Minister of Finance. The request was granted and interviews took place on January 25th and February 11th and 12th. Several differences of opinion developed regarding details, some of which were carried before the Privy Council, but a thorough revision of the banking law was enacted and received the royal assent on May 16, 1890.[2] The important features of the Canadian banking system, as it developed from the legis-

[1] "Although the liquidators were ready to redeem within a month, the discount on the notes of the Exchange Bank after its failure rose as high as five or ten per cent. Redemption of the notes of the Maritime Bank, though finally in full, was delayed for nearly three years after the failure, and in the meanwhile its issues sold for as low as forty cents on the dollar. In notes of the Central Bank of Canada, Americans near Sault Ste. Marie found a profitable speculation by buying them up after the failure, at ten per cent. discount."—Breckenridge, 315.

[2] 53 Victoria, c. 31, "An Act respecting banks and banking."

lation of 1870 and 1880 into that of 1890, may be discussed under the following headings:

1. Security of note issues.
2. Elasticity of circulation.
3. Uniformity of circulation, without discount upon the notes.
4. Inspection of accounts and security of general creditors.
5. Cash reserves and the use of coin.
6. Branch banks and the requirement of large capital.

I. The essential conditions which secure the note issues of the Canadian banks are the duplicate liability of shareholders, the first lien of note-holders upon the assets of a failed bank, the Bank Circulation Redemption Fund, and the six per cent. interest which accrues upon the notes of failed banks from the date of refusal to redeem to the date when readiness to redeem is again announced. The duplicate liability of shareholders dates back to 1834 in Ontario and 1841 in Quebec. The making of the notes a first lien on the assets was suggested by the bankers in 1869, but was abandoned because of the opposition of Mr. Hincks. He feared that the impairment of the equal claims of other creditors which this provision involved would lead to a run by depositors and to the injury of the banks. The failures between 1874 and 1879 compelled many note-holders to realize on their notes at a great discount, in order to obtain immediate use of their money,[1] and dissatisfaction was so great that the bankers again proposed in 1880 that the notes be made a first lien. The total assets of each bank were from six to ten times its note obligations and, if these assets were lost, the duplicate liability of the shareholders would still cover the outstanding notes. These resources constituted a security for the redemption of the notes which it was believed would prove complete, and which the bankers were willing to concede to the public for the privilege of retaining unimpaired their power of note issue.

The Act of 1890 confirmed the provisions of 1880 for making the notes a first lien on the assets, and added two

[1] Breckenridge, 289.

new provisions designed to keep the notes of a failed bank absolutely at par during the period of liquidation. The most important of these was the creation of a safety fund, to be called "The Bank Circulation Redemption Fund," which was to be raised by contributions from the banks, before July 16, 1892, to an amount equal to five per cent. of the average circulation of each contributing bank. The redemption fund is in the custody of the Minister of Finance and bears interest at the rate of three per cent. per annum. It is specifically set apart for the payment of the notes of failed banks. Redemptions are required to be made without regard to the amount which the failed bank may have paid into the redemption fund, but when the redemptions, with interest, exceed such payments, the Minister of Finance may call upon the other banks to make good to the fund the amount of such excess. These calls upon the other banks are limited to one per cent. annually of the amount of their circulation and the amounts thus paid by the banks are reimbursed to them when recovered from the failed bank.[1]

The redemption fund afforded a guarantee, if it was needed, that the notes of a failed bank would always be paid in full. A further provision was made that the notes of failed banks should bear interest at the rate of six per cent. per year from the day of suspension to the date named for their payment. The practical operation of this provision has been eminently successful and has, in connection with the guarantee afforded by the safety fund, made the notes of a failed bank as valuable an investment up to the time of redemption as a six per cent. bond. The holders of such notes have had no difficulty in selling them at par to the other chartered banks, to brokers or to persons having a little

[1] The omission of a limitation of this sort upon the liability of the banks for the general safety fund was one of the causes of hostility to the banking plan of Secretary Carlisle, presented to the United States Congress in his annual report for 1894. It was admitted by those familiar with the facts that the resulting calls were not likely to be large in fact, but it was feared that the indefinite character of the liability would excite alarm among depositors.

money seeking temporary investment. The legal money of redemption under Canadian law is "specie," and the gold standard is maintained with but little gold in circulation. The banks, in making ordinary payments, were required by the law of 1880 to pay amounts up to $50, upon request of the payee, in Dominion notes. This limit was raised in the Act of 1890 to $100.

2. One of the important benefits inherent in the Canadian bank-note circulation is its elasticity. This is not due affirmatively to recent legislation, but is due to the successful resistance of Canadian bankers to government propositions for a specially secured currency.[1] The banks pay out the notes when business activity demands them and the notes drift back for deposit and the settlement of discounts when business activity slackens. The circulation thus varies nearly fifteen per cent. in the course of a year. The minimum circulation of the year has ranged during the past thirteen years from $28,063,000 in 1884 to $31,927,000 in 1893, while the maximum circulation of the year has ranged from $33,998,000 in 1884 to $38,688,000 in 1892. The month of October has been, with one exception during the past thirteen years, the month of maximum circulation. The minimum has been reached in some cases in April, and in others not until July or August, but the larger part of the reduction occurs during the spring and promptly upon the contraction of the demand for money. The following table, showing the maximum and minimum circulation, with the month in which it has occurred, for the past seven years, affords an illustration of the fluctuations:

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[1] Even in 1890 the theory of a circulation based upon evidences of the public debt had considerable footing and was advocated by Sir Donald Smith, President of the Bank of Montreal. It seemed to be thought in Canada that such a system would benefit the larger banks at the expense of the weaker and some of the opposition to the creation of a safety fund was apparently based upon the fact that it would invest the notes of the weakest banks with the same credit as those of the strongest.—Breckenridge, 320. This argument was necessarily directed against convenience and uniformity.

YEAR.	LOWEST POINT.		HIGHEST POINT.	
	MONTH.	AMOUNT.	MONTH.	AMOUNT.
1888	May	$29,278,000	October	$36,244,000
1889	May	30,012,000	October	35,233,000
1890	April	30,672,000	October	36,480,000
1891	July	30,580,000	November	37,431,000
1892	May	31,383,000	October	38,688,000
1893	May	31,927,000	October	36,906,000
1894	May	28,467,000	October	34,516,000

The banking experience of Canada in recent years is a sufficient vindication against the charge that a banking currency leads to inflation. The volume of notes usually in circulation exceeds by only a small fraction fifty per cent. of the aggregate capital stock of the banks, although they are allowed to issue to the full amount of their capital. Some of the banks have occasionally touched the maximum limit and the branches have been promptly notified by telegraph when the limit has been reached. A real demand for money from such banks is met by loans to them from banks which have not reached the limit. The contracts for these loans call for money, like other contracts, but it is understood that they shall be paid in the notes of the lending banks, so that the public get the benefit of the limit upon their combined issues and the two banks divide the profits on the circulation thus put in circulation.[1] The paid-up capital of the Canadian banks on January 1, 1896, was $62,196,391, and the notes outstanding were $32,565,179, so that there was a margin of issues unavailed of to the amount of nearly $30,000,000.

3. The necessity of providing more fully for maintaining the notes of all the banks at par in all parts of the Dominion, which was recognized in 1890, was due not so much to any question of the solvency of the banks as to the mechanical provisions for redemption. The convenience of note-holders had already been partially provided for by mu-

[1] Root, *Canadian Bank-Note Currency*, "Sound Currency," II., No. 2, p. 7.

tual arrangements between the banks for the redemption of each other's notes. It would have involved a manifest injustice, in view of the wide difference in character and strength of the Canadian banks to compel each to redeem the notes of all others against its will, but the banks were ready to accept a mandatory law requiring each bank to establish agencies for the redemption of its own notes at the commercial centre of each province. It was accordingly provided in the Act of 1890 (Section 55) :

> The bank shall make such arrangements as are necessary to ensure the circulation at par in any and every part of Canada, of all notes issued or reissued by it and intended for circulation ; and towards this purpose the bank shall establish agencies for the redemption and payment of its notes at the cities of Halifax, St. John, Charlottetown, Montreal, Toronto, Winnipeg, and Victoria, and at such other places as are, from time to time, designated by the Treasury Board.

4. The bank-note circulation of Canada, under the operation of the redemption fund and the complementary requirements, has, in the language of Mr. Breckenridge, "acquired a thoroughly national character ; since 1890 it has circulated from one end of the country to the other, never causing loss to the holder, yet keeping unimpaired the qualities for which, in its less perfect state, Canadians had again and again refused to give it up."[1] The fulfilment of these conditions, with the elasticity and sufficiency which usually accompany a banking currency, meet all the requirements of a perfect currency system. The protection of the note-holder against both temporary and permanent loss closes the case in favor of Canadian banks of issue. They may be well or ill managed as banks of discount and deposit, but, as such banks must exist under any currency system, their bad management cannot be made an argument against the power of note issue unless that power increases their power for evil as banks of discount and deposit. Questions, therefore, relating to the management of the Canadian banks in their discounting business, and the number of failures they may have suffered, should not be confused with the question

[1] *The Canadian Banking System*, 338.

of the success of their system of note issues in providing a sufficient, elastic, and secure currency.

Having made this distinction, it may be admitted that the Canadian banking system is capable of improvement in the direction of official supervision. While discount banking is essentially a private business, it is usually done by corporations holding special privileges by authority of the state, and the subdivision of modern industries justifies the citizen in asking that the state exercise the power of visitation and supervision over such corporations, when they deal intimately with the public, which he cannot conveniently exercise for himself. The weakest spot in the Scotch and Canadian banking systems has been the absence of this supervision, and, defective as government supervision often is, it would probably have prevented some of the great losses which have come to shareholders in those countries. The proposal of government supervision in Canada has been several times brought before Parliament, but has always been resisted upon the grounds that public auditors or inspectors could not ascertain accurately the real character of banking assets, and that the fact of government inspection would mislead the public into a confidence which might prove to be misplaced. The project of inspection was renewed by Mr. Foster in 1890, but the auditors whom he proposed were to be appointed by the shareholders at their annual meeting. The same objections which had been made on previous occasions were renewed and the project of a formal audit was again abandoned.

The larger Canadian banks are not, however, without a system of supervision of their own, which ought to be more efficient than that of government officers when there is no collusion between the inspector and general manager. Such collusion is not likely to be a frequent occurrence, because the chief inspector is required by his duties to be a man of independent judgment, of banking experience and reputation, and to receive a large salary. It is his duty to make tours of the branches, annually or oftener, for the purpose of examining the character of the discounts granted and the

general policy pursued. The mere verification of accounts is performed by subordinates. The chief inspector, therefore, is the equal in character and position of the general manager, and is exposed to few of the temptations of an inferior. He confers with the latter and reports the results of his inquiries regarding the standing of firms seeking discounts. If the inspector is associated too closely by family or other ties with the general manager, the fact is likely to become a subject of business gossip and to impair confidence in the bank. The establishment of the general redemption fund has had a salutary effect in attracting the attention of the banks to each other's condition, because of the common responsibility which the fund imposes.

The safeguards of the Canadian system have been such that the entire losses to creditors, exclusive of shareholders, since confederation in 1867, have been less than $2,000,000, representing an average of about $72,000 annually, or $1 in $3000 of the present average liabilities. "The record for the years preceding 1867," says Mr. Breckenridge, "is hardly less admirable, there being no failures in Nova Scotia or Lower Canada, while in New Brunswick the double liability of shareholders saved the banks' creditors, and in Upper Canada the failure of the Bank of Upper Canada was the only one which inflicted considerable loss."[1] The Bank of Upper Canada violated the rules of sound banking under the stimulus of a period of rapid growth in Ontario, and made heavy loans to lawyers, politicians, and the gentry. Much money was lost in the land speculations of 1857, the capital was reduced in 1861, the public deposits were reduced in 1863, another reduction of capital in 1866 failed to save the bank, and payment was stopped September 18, 1866, with liabilities of $3,402,000. The assets were nominally worth $5,362,000, but gradually shrunk until in 1882 they were only $420,387 against still outstanding liabilities of $1,380,015. Of this liability $1,122,649 was still due the government, which was open to the suspicion by its tardy efforts to re-

[1] *The Canadian Banking System*, 355

cover that it had abused its power to obtain advances from the bank during its period of prosperity.[1]

Six failures occurred in Canada between 1871 and 1881, six between 1883 and 1889, and two after the latter date. The notes in every case since 1881 have been paid in full, but in some cases prior to 1890 they were redeemed after considerable delay and after they had fallen to a discount. The capital of only one of the failed banks was larger than $500,000. This one was the Federal Bank of Canada, which increased its capital in 1883 to $3,000,000, but was compelled to reduce it in 1885 to $1,250,000 on account of losses from Michigan lumber transactions and loans in Manitoba. There was no panic in the case of any of these failures, and the other banks having offices in Toronto came to the assistance of the Federal Bank in January, 1888, and agreed to advance enough money to pay off its entire liabilities and assume the assets, if the bank would wind up its affairs. The shareholders in Canadian banks lost between July, 1867, and the close of the year 1889 $23,000,000 in capital, accumulated reserves, and assessments resulting from duplicate liability.

The two failures since 1890 have been those of the Commercial Bank of Manitoba and the *Banque du Peuple* of Montreal. The Commercial Bank succeeded to the business of a private firm at Winnipeg in 1884 and assumed the heavy risks which are often run by banks in new countries. Its business was essentially local and its failure was not a surprise to other bankers in the Dominion. The other banks were critical as early as 1892 about accepting the drafts of the Commercial Bank on Montreal, and in May, 1893, a drain of deposits began. The bank paid out its notes for a time to nervous depositors and thus increased its circulation between May 31st and July 3d by the sum of $140,605, while the deposits were reduced $189,813.[2] The automatic

[1] Breckenridge, 175.

[2] The purpose of depositors in accepting their deposits in notes was to convert an ordinary claim into a preferred claim, but the process of conversion was necessarily limited by the limit of circulation allowed the bank, as well as by the certainty that the bank would quickly be unable to settle its balances with the other banks.

operation of the Canadian system of redemption came into play when these notes fell into the hands of other banks, and the Commercial Bank was compelled to suspend with liabilities of $1,344,269. The *Banque du Peuple* was compelled to reduce its capital in 1885 from $1,500,000 to $1,200,000, and suspended on July 16, 1895, with a circulation of about $787,000 and with total liabilities of about $7,500,000.

The *Banque du Peuple* closed its doors in the hope that arrangements might be concluded with its creditors which would enable it to resume business within the period of ninety days, for which continued suspension would, under the law, "constitute the bank insolvent and operate a forfeiture of its charter or act of incorporation, so far as regards all further banking operations."[1] The notes remained steadily at par and were redeemed before October 5th, except $150,000, for which the money was held in the bank. One of the plans proposed for reorganization was the issue of deposit receipts to depositors, payable in from six months to two years. The period of suspension passed, however, without resumption, and it appeared at the meeting of the shareholders on December 17, 1895, that overdrafts had been granted to five individuals and firms amounting to $1,229,000, and to four of the directors to the amount of $235,000. The cashier was among those to whom large overdrafts had been granted, and it was reported that he had allowed the auditors only twenty hours to examine transactions aggregating $26,000,000 and had misled both auditors and directors.[2]

5. The requirement of a fixed minimum reserve of specie against liabilities was suggested by Mr. Hincks in 1869, but he was convinced by the unanimous opposition of the bankers that the requirement would prove more of an injury than a benefit to the business community in times of stringency. It was pointed out that a reserve which cannot be used is of no avail in emergencies; that if the proportion were low, it

[1] Sec. 91.

[2] *New York Evening Post*, Dec. 18, 1895, special despatch from Montreal.

would be treated by weak banks as always sufficient; and that a part of a bank's best and most available funds often consisted of balances in New York and London, rather than specie in its own vaults. These arguments were conclusive with Mr. Hincks, but they failed to convince Mr. Foster when the plan of a minimum reserve was suggested to him in 1890. The experiment of a minimum reserve had then been longer in operation in the United States and was believed to have produced beneficial results. It was pointed out, however, that the small local banks of the United States occupied a very different position from the great chartered banks of Canada and that regulations which might be necessary in the one case might not be in the other. Mr. Foster's proposition was to require each bank to hold specie and Dominion notes to the amount of ten per cent. of its liabilities. The bankers carried the contest before the Privy Council and at a hearing given them on February 22, 1890, carried the majority with them and secured the exclusion of any provision for the reserve from the government bill.[1]

One of the strongest arguments in favor of liquid reserves and banking upon general assets, without government interference, is found in the comparative calm which has reigned among Scottish and Canadian bankers when those of other countries have been shaken by panic. The last test of this kind came in 1893, when Canada could not fail to be affected by the acute financial convulsion of her great neighbors, the United States. Four of the Canadian banks have their own offices in New York and the others have agents there as well as in London. These agencies do not seek business actively in New York and London, but buy and sell bills of exchange when they can do so to better advantage than the parent bank. They loan more or less on call, but only rarely on time. In periods of stringency they have several times come to the rescue of the New York money market, when the requirements of a rigid reserve law tied the hands of the American banks. Their most important service has been, however, to their parent banks when the pressure of an

[1] Breckenridge, 327.

unusual demand has led the latter to draw upon their foreign balances. These balances in New York constituted one of the best liquid assets of the Canadian banks in 1893 and were drawn down nearly $8,000,000. The banks sacrificed temporary high profits, raised their interest rates no higher than seven per cent., protected their regular customers, and while their neighbors across the border were foundering in the waves of a financial crisis, they rode the storm with a serenity which might have justified for them the heroic motto of William the Silent, *Sævis tranquillus in undis*.[1]

6. Two of the important features of the Canadian, as well as of the Scotch banking system, are the large capital required by the banks and their system of branches. While each feature is capable of separate discussion, they are more or less connected with each other, from the fact that the requirement of a large capital limits the number of the banks and makes the establishment of branches necessary to afford banking facilities to the country. The minimum paid-up capital required in Canada prior to the revision of 1890 was only $100,000, and several small banks of a local character had failed and caused losses to the depositors as well as the shareholders. The law of 1890 required subscriptions to the capital stock of each new bank to an amount not less than $500,000 and actual payments to the amount of $250,000. No new bank is permitted to begin business or to issue notes until the Treasury Board is satisfied that this capital has been actually paid up, and only two banks are now in existence chartered since 1883. The paid-up capital of the thirty-eight Canadian banks on December 31, 1895, was $62,196,391, of which $52,608,489 was in Ontario and Quebec. This affords an average about nine times as large as that of the 3715 national banks of the United States, which reported a capital on November 1, 1895, of $664,136,915. The Bank of Montreal now has a paid-up capital of $12,000,000; the Merchant's Bank of Canada, situated at Montreal, and the Canadian Bank of Commerce at Toronto have a capital of $6,000,000 each; the Bank of British North

[1] Breckenridge, 451.

America has a capital of $4,866,666; the Bank of British Columbia has a capital of $2,920,000; the Quebec Bank has a capital of $2,500,000; Molson's Bank of Montreal has a capital of $2,000,000; and the Imperial Bank of Canada at Toronto has a capital of $1,963,600. The smaller banks are in Nova Scotia and New Brunswick or among the French banks of Quebec which received charters at an early date. The smallest paid-up capital is that of the Summer Side Bank of Prince Edward Island, which is $48,666. The thirty-eight Canadian banks had at the beginning of 1896, outside of city branches of local banks, 483 establishments in 273 localities. There were 250 bank offices in Ontario, 89 in Quebec, 63 in Nova Scotia, 31 in New Brunswick, 20 in Manitoba, 14 in British Columbia, 9 in the Northwest Territory, and 7 in Prince Edward Island.[1] The entire country is thus served as efficiently in the mere number of establishments as the United States with its banks without branches.

It is maintained by the friends of the Canadian system that the combination of large capitals and numerous branches has many advantages beyond the mere supply of banking facilities. It secures on the one hand a unity of policy on the part of the leading banks in times of stringency far different from the playing at cross-purposes which distinguished the action of the national banks of the great reserve cities in the United States in the panic of 1893 against the smaller banks of the interior and the far West. The Canadian system, on the other hand, does not sacrifice one section to another, but enables the managers of the large banks to distribute accommodation evenly throughout their system, to mass currency where it is most needed, and by means of their power of note issue to equip every branch with ample resources for sustaining commercial credit without weakening their reserves of actual cash. The effect of the Canadian system has been to make the rate at the most distant interior

[1] Letter of Mr. J. H. Plummer, Chairman editing committee of Canadian Bankers' Association, January 31, 1896.

branch not more than one or two per cent. higher than to the best borrower in Montreal or Toronto, while in the United States rates range between ten and twelve per cent. in the newer sections of the country while money is a drug in the market in the great reserve cities.[1] The effect of the comparative unity of Canadian banking without the evils of monopoly which sometimes accompany such unity, is to diminish failures and protect a bank against local losses by the profits in other localities. The management at the central office are able to keep a sufficiently close watch upon every branch to prevent reckless banking and bad management, but they are willing to conduct a branch in many cases at a rate of profit which would not justify the maintenance of a separate bank or even of a branch bank without the power of note issue. The Canadian system, therefore, permits the extension of banking facilities more efficiently than the American system of small independent banks, and the power to issue notes against general assets affords a margin of profit and a diminished expense for cash reserve which would not be afforded by a specially secured note issue.

The leading items of the accounts of the Canadian banks for representative years have been as follows:[2]

[1] Cornwell, 16.

[2] The table gives only a general view of the progress of Canadian banking operations, without permitting absolutely exact comparisons, because of the changes in the form of the official reports which were made in 1870, 1872, 1880, and 1890. The figures for 1841 and 1851 are reduced from pounds sterling, in which the accounts were then expressed, and with those of 1861 cover only the Dominion of Canada, without including New Brunswick and Nova Scotia. The changes in the form of statement affect principally the item of discounts, which included substantially all loans in 1867, but excluded certain advances on securities and on current accounts between that date and 1890. The present form of statements includes under "current loans" somewhat more than was formerly included. In every case, however, these loans on bills discounted make up the bulk of the loan account. The private deposits in the banks, payable on demand, on December 31, 1895, were $67,452,397; deposits payable after notice or on a fixed day, $119,667,176.

DEC. 31ST.	NO. BANKS.	PAID-UP CAPITAL.	NOTE CIRCULATION.	DISCOUNTS.
1841	9	$11,380,000	$ 455,000	$ 16,400,000
1851	8	14,480,000	810,000	27,800,000
1861	16	24,410,796	11,780,364	39,588,842
1867	28	32,500,162	10,102,439	54,899,142
1873	28	57,931,359	29,016,659	119,647,350
1876	39	66,137,315	23,275,701	122,562,334
1880	36	59,819,603	27,328,358	105,587,672
1885	41	61,763,279	32,363,992	125,493,660
1890	38	60,057,235	35,006,274	153,236,184
1891	38	61,299,305	35,634,129	186,590,602
1892	39	61,938,515	36,194,023	198,532,160
1893	39	62,099,243	34,418,936	200,397,498
1894	39	61,683,719	32,375,620	195,836,141
1895	38	62,196,391	32,565,179	202,088,259

CHAPTER XVII.

THE BANKS OF LATIN AMERICA.

Variety of Systems in Mexico and the Southern Countries—The Experience of Chile, Brazil, the Argentine Republic, and Uruguay, with the Suspension of Specie Payments—Paraguay and the Northern States—Haiti, Central America, and the Banks of the European Colonies.

THE banking systems of the American States and dependencies of the South offer a great variety of methods of note issue and a great variation in the safeguards thrown around such issues. Some of the banking systems of Latin America have been the development of time and experience; others have been framed as an entirety upon the model of some European system, sometimes with the approval of eminent foreign economists; and others are simply concessions by the governments to English capitalists who conduct the affairs of the banks from London. The domestic systems of banking and of currency have illustrated in many cases the fact that the best regulations do not always constitute a safeguard against unsound banking in countries where internal development is rapid, speculation is intense, and the conservatism of fixed conditions does not prevail. Bad as have been the results of some of the banking systems, however, their evils have hardly kept pace with the evils of government paper currency, which has proved such a fetter upon the prosperity of many South American States. The banking systems which have been at their worst have been those which have been only covert branches of the Treasury or the pliant tools of executive

power. The banks founded by English capital have for the most part kept free from these entanglements and have paid continuous dividends to their shareholders. They have not escaped in some cases serious losses from the depreciation of the paper currency or the fall of exchange in silver-using countries, but they have battled against these evils with the intelligence and caution which are derived from a knowledge of correct banking principles.[1]

The Banks of Mexico.

The present banking circulation of Mexico is principally supplied by the National Bank of Mexico, which grew out of the consolidation in 1884 of several banks of issue then in existence. Several banks were authorized to issue circulating notes under special charters during the early history of the republic, but only a few survive, one of these being an

[1] The great English banks which do business in South America, as well as in Asia, Africa, and the islands of the sea, are one of the potent instruments of British commercial supremacy in the world and concentrate the business of foreign exchange in London. Sixty incorporated banks, nearly all of large capital, exist in London, devoted exclusively to international banking. Their aggregate capital is computed at $294,000,000, in addition to $175,000,000 invested by private banking houses, and their deposits exceed $1,200,000,000.—Address of Ulysses D. Eddy before National Association of Manufacturers at Chicago, *New York Journal of Commerce*, Jan. 24, 1896. The International American Conference, held at Washington in 1889, recommended the creation of an international American bank, to promote direct exchange transactions with South America. Bills have been introduced in several successive Congresses, proposing the incorporation of such an institution, and one is pending in the Fifty-fourth Congress, but no effective action has yet been taken. It was suggested by Secretary Blaine, in his letter to President Harrison, transmitting the report of the Conference, in favor of such a bank, that the volume of trade with the countries south of the United States amounted in 1889 to $282,005,057, of which $181,058,966 consisted of imports of merchandise into the United States and $71,938,181 of exports of merchandise, upon which a commission of three-quarters of one per cent. would represent a banking charge of about $1,800,000. —Sen. Ex. Doc. 129, Fifty-first Congress, 1st Sess., 2.

English institution called the Bank of London, Mexico, and South America. The National Bank of Mexico was founded mainly with French capital, and occupies substantially the position of the Bank of England in regulating the credit circulation of the country and making advances to the government. The capital is $20,000,000,[1] of which forty per cent. is paid up. The bank agreed at the outset to advance from $6,000,000 to $8,000,000 to the government at six per cent., and to collect a part of the federal revenues for a small commission. The charter of the bank runs for fifty years from May 31, 1884. The bank has the right to issue notes to the amount of three times the cash reserve, which may be held in gold or silver coin or bullion. Their issue is supervised by two officers appointed by the government, who affix an official seal, indicating that the stamp tax has been paid, and take note of the cash reserve, in order to assure themselves that the law imposing a fixed proportion between reserve and note issues is complied with.

The denominations of the notes run from $1 to $1000 and they are required to be redeemed in silver coin on demand at the central office of the bank or at the branches through which they are issued. The notes of the National Bank are receivable for public dues in cities where branches exist or where there are agents who exchange the notes for coin without discount.[2] The liabilities of the National Bank on account of circulation on December 31, 1895, were $18,359,346 and of the International and Mortgage Bank about $2,000,000. The total liabilities of the National Bank on that date were $67,743,288, of which $24,641,661 was on account of deposits, $1,992,281 on account of reserve, and $20,000,000 on account of capital. The assets included $12,000,000 in capital not called up, $25,695,037 in cash

[1] The Mexican unit is the dollar or peso, which is worth in gold $0.983, but the country is on the silver basis, which makes the silver coins worth only about half their nominal gold value. The amounts in the text are expressed in Mexican silver dollars.

[2] Lévy, 271.

items, $14,133,038 in commercial paper, and $11,372,706 in debtor current accounts.[1]

The Banks of Chile.

Chile has been in recent years under the domination of government paper money and legal tender bank-notes, in spite of the comparative wealth and prosperity of the republic among other South American countries. Free banking existed in Chile up to 1839, when a law was passed forbidding the creation of banks of issue without the authority of the governor of the municipality or department where they were established. A general reform of the banking system was made by the law of July 23, 1860, under the inspiration of M. Courcelle-Seneuil.[2] This law limited the maximum circulation to one and one-half times the capital of the banks and provided that the notes should be redeemable in specie, and in case of default should constitute a judgment (*titres exécutoires*) against the goods and persons of the proprietors. The issue of the notes was placed under the supervision of the public authorities by requiring the signature and seal of the superintendent of the mint. Shareholders were liable only for the amount of their shares, loans to officers and directors were required to be specially recorded, and the books and cash were to be open to government inspection.[3] These regulations are still in force, but the readjustment of the monetary standard has led to some recent changes in the provisions governing the circulation.

The suspension of specie payments in Chile was decreed in 1865, but was brought to an end on August 31, 1866. The specie basis was again abandoned and forced legal tender decreed by a law of July 25, 1878, which fixed the maximum circulation at 15,000,000 piasters ($13,600,000), divided among eleven banks which subscribed to a new loan. The

[1] The author is indebted to Señor Romero, the Mexican Minister at Washington, for the latest figures from the *Diario Oficial*, Jan. 3, 1896.

[2] Lévy, 291.

[3] Comptroller's Report, 1895, Letter of Minister Edward H. Strobel, 68.

government resorted to legal tender paper, issued directly by the Treasury, during the war with Peru, and the amount had risen, on January 5, 1881, to 40,000,000 piasters. The banks, at the outbreak of the revolution against President Balmaceda in 1891, had a circulation of about 15,000,000 piasters, upon a capital of 30,000,000 piasters and a reserve of 6,000,000. The circulation increased after the fall of Balmaceda to 20,000,000 piasters, and the government paper money increased to 42,000,000 piasters. The Junta established at Iquique during the civil war proclaimed liberty of note issues, and the Bank of Tarapaca, the railway companies, the municipality of Iquique, the principal corporations and business houses, and even retail tradesmen, issued their own notes. The notes were not legal tender and the public accepted those they regarded as good and rejected those they regarded as bad, but the return of civil order was followed by the redemption of the paper in nearly every case. The government made an unsuccessful effort to restore specie payments in 1892, by means of a bond issue and an adjustment of the standard to meet the depreciation of the paper money. The paper continued at a heavy discount and a new law was pushed through Congress early in 1895, still further reducing the standard. The "dollar" was made the monetary unit, but was reduced to one-thirteenth part of a pound sterling or about 36.49 cents in United States gold coin. Gold was made the monetary standard and was to be paid out for paper, beginning June 1, 1895. Resumption was begun under these requirements, but the foreign exchanges were for some time unfavorable and gold was largely exported.

The law of 1895 put a limit of 24,000,000 dollars ($9,000,000) upon bank-note issues until December 31, 1897, apportioned to the paid-up capital of the banks, and provided that the notes should be guaranteed to their full amount by deposits in the public treasury of gold, government notes, municipal bonds, treasury bills, or bonds of mortgage banks. These notes are to be receivable in payment of taxes until December 31, 1897. The notes constitute the first lien on

the assets, and in case of failure the securities in the treasury are to be sold for the benefit of the note-holders.[1] The total circulation of the Chilean banks on August 31, 1895, expressed in Chilean money, was $19,304,386, deposits were $114,228,282, and gold holdings were $3,557,695. The Bank of Chile, by far the largest institution in the country, had on August 31, 1895, $10,639,595 in outstanding notes, $50,705,626 in deposits, and a paid-up capital of $20,000,000. Its advances and amounts receivable were $64,374,979 and its cash, including government notes and checks, was $8,995,213.

The Banks of Brazil.

The government of Brazil succeeded in 1888, before the overthrow of the Empire, in restoring the parity of the paper currency based upon the gold standard. The milreis was worth fifty-four and six-tenths cents in United States currency, and foreign exchange was substantially at par. The circulation at the time of the fall of the Empire in 1889 was about 200,000,000 milreis ($109,000,000) in paper. Two banks were founded at about this time with the support of French capitalists,—the National Bank of Brazil and the Bank of the United States of Brazil. They had been in operation but a short time when a decree of President Fonseca in December, 1890, based upon a report by Ruy Barbosa, the Minister of Finance, authorized the union of the two institutions under the name of the Bank of the Republic of the United States of Brazil, with a capital of 200,000,000 milreis. The new bank was authorized to issue notes to three times the amount of its gold reserve, and the charter provided that the government should grant the right of note issue in future to no new banks and that the circulation of existing banks should be remitted to the new establishment as the old ones surrendered their privileges. The existing banks of issue numbered six, with a limit of circulation of 166,000,000 milreis. The new bank undertook

[1] *Bulletin of the Bureau of the American Republics*, April, 1895, 670–74.

the retirement of the government paper money, which had been in circulation for some fifteen years and still amounted in June, 1891, to 168,000,000 milreis.

A new organization was given to the Bank of the United States of Brazil by an Act of December 17, 1892, under the title of the Bank of the Republic of Brazil. The capital was reduced from 190,000,000 milreis to 150,000,000 milreis, the notes were made legal tender, and the bank was pledged to retire 100,000,000 milreis in bills within the year 1893.[1] The circulation of the bank, including interest-bearing bonds, which were made legal tender and receivable at public depositaries, and including the circulation of other bank bills assumed by the consolidated bank, reached 379,390,720 milreis ($205,000,000) and the government paper money reached 200,000,000 milreis ($109,000,000)[2]. This was the situation early in 1893, but the suspension of specie payments as the result of a new civil war led to repeated new issues of paper money and a constantly growing premium on gold. The pledge to retire paper money and bank-notes in 1893 was partially kept, only to be followed by new issues larger than those withdrawn. The total circulation was thus forced up early in 1894 to 713,000,000 milreis,—of the nominal value of $385,000,000 in United States money, but an actual value of much less,—but some reduction was made during 1894 and 1895, and the paper circulation was computed in the latter year at 340,711,370 milreis in bank-notes and 367,358,652 milreis in government notes.[3] The statutes establishing the bank provide for the resumption of specie payments as soon as foreign exchange has been maintained for one year at par or as soon as the forced legal tender of the bills shall be suspended. The government, however, has employed the deposits of the banks for war expenses and resumption does not seem to be at hand. Foreign commerce has enjoyed the benefit which is attributed to an unfavorable exchange in stimulating exports, but in 1892 the rise of prices in dispro-

[1] *Revue des Banques*, January, 1893, XII., 293.
[2] Lévy, 282–84.
[3] *Revue des Banques*, July, 1895, XIV., 141.

portion to wages drove Italian and other European laborers out of the country to such an extent that coffee planting could not command the necessary number of hands.[1]

Banking in Argentina.

The forced legal tender of paper currency is declared by M. Lévy to have been, "since 1826, a chronic malady, with rare intermissions, in the Argentine Republic."[2] The history of the country for the years prior to the crisis of 1890 was the story of unduly expanded credit, discounting too rapidly the possibilities of the future, which was witnessed in the United States in 1837 and 1857 and more recently in Australia. The oldest bank of the Argentine Republic was the Bank of the Province of Buenos Ayres, which was founded as a private bank in 1822, but was purchased by the State in 1826 from the proceeds of an English loan. It was authorized as a state bank to issue circulating notes redeemable in silver. The issues were excessive and had depreciated in 1868 to a value of four cents on the dollar. The bank was then authorized to convert the notes into a new issue and continued in operation until 1891. The Bank of the Nation (*Banco de la Nacion*) was created by the Act of November 5, 1872, limiting the circulation to double the paid-up capital and requiring a cash reserve of at least one-fourth of the outstanding notes. The government subscribed for $2,000,000 of the capital stock, which was fixed at $5,000,000.[3] The bank was given continuance for twenty years and its notes were legal tender.

The banking system which was established in 1887, and which broke down so completely in 1890, was peculiar in the fact that the circulating notes purported to combine the double guarantee of metallic coverture, so dear to the fram-

[1] London *Bankers' Magazine*, January, 1893, LV., 79.

[2] *Mélanges Financiers*, 286.

[3] The Argentine monetary unit is the peso ($.965), equal to five francs, but its value is so near that of the dollar that Argentine currency is often stated in dollars.

ers of the English Act of 1844, and the coverture by means of evidences of the public debt, which is the basis of the national banking system of the United States. But the gold was borrowed, the issue of evidences of the public debt went beyond legitimate currency requirements and the guarantees proved of no avail against inflation, depreciation, and resulting insolvency. The Bank of the Nation was reorganized under the Guaranteed Banking Act of November 3, 1887. This Act authorized the issue of notes by any provincial bank which complied with the requirement of a deposit of government bonds. A special issue of four and a half per cent. gold bonds was authorized by the general government as the basis of this circulation, and in order to secure the gold required to buy these bonds each of the provinces desiring a provincial bank sold abroad a special issue of its own gold bonds. The gold received was paid into the national Treasury for the national bonds and the banks of the provinces were authorized to issue an amount of paper money equal to the bonds thus purchased. The provinces became responsible for the issue of paper money by the respective provincial banks.[1] A considerable sum of gold was obtained by the sale of bonds, which resulted in a great inflation of the prices of property on which loans were made by the banks.

Bad banking and excessive issues wrecked the new system within four years, and sent gold to 300 per cent. in paper, in spite of the security of the note issues. Every bank of issue suspended in 1891 and is still in process of liquidation. The guaranteed bonds issued to found the system were estimated to be outstanding in 1893 to the amount of $100,082,965.[2] The inflation had been aided by the issue of paper money without special guarantee, but it was the opinion of the executive power that the Guaranteed Banking Act was the cause of the crisis.[3] The government as-

[1] Comptroller's Report, 1895, Letter of Minister William I. Buchanan, 596.

[2] London *Bankers' Magazine*, March, 1893, LV., 408–16.

[3] Lévy, 286.

sumed responsibility for the outstanding paper and required the surrender of the bonds and specie held by the banks. It was necessary to have some banking institution to permit the continuance of government finance, and the Bank of the Argentine Nation was erected in December, 1891, upon the ruins of the old Bank of the Nation and of the provincial banks. The bank was opened with a capital of $50,000,000, entirely paid in paper. The affairs of the old national bank were made over to the new bank and its shareholders given a preference in the subscriptions to the new stock. The bank was allowed to issue notes to the amount of seventy-five per cent. of the internal bonds deposited as a guarantee.[1] The attempt to sell stock to the public proved a failure and the capital of the bank was furnished exclusively by the Treasury.

Banking in Paraguay.

Banking in Paraguay has been in a somewhat chaotic state since the collapse of credit in the Argentine Republic, of which the country is a near neighbor. The circulation was issued for many years by the National Bank of Paraguay, in which the government was a large shareholder. The gold unit of value, prior to the suspension of specie payments, was the English pound sterling, and five paper dollars were paid for £1 in gold. The suspension of the National Bank of the Argentine Republic on January 1, 1885, was not followed at once by suspension in Paraguay, but later in the year gold went to a premium of fifty per cent. The National Bank had the option of redeeming in gold or silver, and redeemed in silver until 1889, when the Bank of Paraguay and the River Plate was founded, redeeming its notes exclusively in silver. Both banks were subjected to a severe run in 1890, their silver reserves were reduced, and gold went to 300 per cent. in paper. The National Bank suspended the payment of its obligations and announced that it would be compelled to grant an extension to its customers, many of whom were land owners of

[1] London *Bankers' Magazine*, June, 1892, LIII., 905.

large means, but unable to meet their immediate obligations. The bank was granted by law a ten years' extension of time within which to collect its credits and settle its debts, and debtors were expected to pay their indebtedness in quarterly instalments during the ten years. The money had originally been borrowed upon a specie basis, but was to be paid back in paper. Even these payments were not made, and in August, 1894, the bank agreed to accept fifty per cent. of the amounts due. Many debtors paid under this condition, but the demand for money drove up the interest rates so sharply that others were prevented from making payment within the three months allowed.[1] The affairs of the bank are now in process of liquidation through a syndicate.

The Bank of Paraguay and the River Plate (*Banco Paraguay y de la Plata*) was founded with a capital of $8,000,000 in Paraguayan money, worth at the time of its foundation in 1889 about 66⅔ cents to the dollar in gold, but now worth about eighteen cents. The government subscribed one-quarter of the capital through a bond for £400,000 negotiated at six per cent., and receives five per cent. of the profits of the Bank of Paraguay in compensation for the privileges of the charter. The present paper circulation of Paraguay is about $5,000,000, with a gold value of about $850,000. The only provision now in force for the redemption of notes is through the customs, of which five per cent. are set aside for redemption purposes. There is a difference of opinion in Paraguay whether to destroy the notes thus redeemed or to employ them in the purchase of gold. The business is managed by the Agricultural Bank (*Banco Agricola*), which is an institution under the entire charge of the government and is governed by a directory of five members named by the executive.

Banking in Uruguay.

Uruguay was until recently under the *régime* of free banking and is still upon the gold basis. There was in circula-

[1] Letter of Vice-Consul Eben M. Flagg, Comptrollers's Report, 1895, 92.

lation a considerable issue of government paper money, but it was entirely withdrawn at the end of September, 1892. The country has made several experiments with government banks, but they have been mismanaged and have gone out of existence. The National Bank was the last of these institutions. The circulation on September 30, 1893, was 780,000 piasters ($800,000) and that of the London and River Plate Bank was 2,600,000 piasters, which was increased a year later to 2,940,000 piasters. The law of March 23, 1865, prescribed uniform rules for the government of banks of issue. One of these rules fixed the circulation at three times the capital, but this was limited in 1870 to twice the capital actually paid up.[1] The private banks in 1893 renounced the right of circulation and it was decided to authorize no additional banks of issue. The two such banks now in existence are the London and River Plate Bank, owned and managed in London,[2] and the Italian Bank of the River Plate. Banks of issue pay an annual patent tax of $2000, which is twice the tax imposed on banks of other classes.[3] The government is not a shareholder in any of the existing banks, but is responsible for the liquidation of the National Bank and named one of the three members of the liquidating committee of the English Bank of the River Plate.[4] Each bank is required to redeem its notes in gold on demand.

[1] Lévy, 281.

[2] This bank does business in several other South American countries, but its issue of circulating notes is limited to Uruguay. The capital of the bank is £900,000, and the current accounts on September 30, 1895 were £9,729,245. The bank carried cash to the large amount of £6,037,411, which was a more effective resource, in the opinion of the chairman of the board of directors, than any form of securities, and had much to do with enabling the bank to weather the storm of the crisis in Argentina, Uruguay, and Paraguay, which swept away so many other banking institutions.—London *Bankers' Magazine*, January, 1895, LIX., 98.

[3] Letter of Minister Granville Stuart, Comptroller's Report, 1895, 105.

[4] The President of the Republic recommended in December, 1895, the creation of a new National Bank, with a capital of $10,000,000, of which a considerable portion is to be sought in London.—London *Bankers' Magazine*, Feb., 1896, LXI., 247.

Bank-notes are not a legal tender, but are a first lien on the assets of the banks and are limited to a minimum denomination of ten piasters ($10.30). The Italian Bank showed total assets on December 31, 1894, of $8,798,570, of which $5,109,197 was in securities and $896,711 in cash. The liabilities were $1,500,000 for capital, $851,230 for circulation, and $5,109,197 for deposits.

The Banks of the Northern States.

Banking in Venezuela is governed by the law of May 7, 1895, which permits the creation of banks of issue under fixed conditions. The notes are not legal tender and can be issued to the amount of no more than fifty per cent. of the paid-up capital. The banks are required to redeem their notes in lawful money on demand, at the central office and the branches. Twenty-five per cent. of the capital of a proposed new bank is required to be held as a cash reserve. The banks of issue are forbidden to loan on their own shares or to make loans which will lock up their capital for over six months. Balance sheets must be published quarterly, showing, among other things, the loans to directors and officers, and changes in the by-laws must be promptly communicated to the government. The national executive is empowered to appoint an inspector for each bank with power to examine books and cash.[1] The only banks in operation are those of Caracas and Maracaibo. Their circulation on December 31, 1894, was 2,382,660 bolivars ($450,000).

The system of government paper currency which prevailed for many years in Colombia has recently been a subject of legislation with a view to raising its value and permitting the creation of a banking system. The law of November 21, 1894, provided for the coinage of silver pieces of ten and twenty cents and the retirement of paper notes of the same denominations. The National Bank was to be reduced to a section of the Treasury Department and its commercial affairs liquidated. The power to issue circulat-

[1] *Gaceta Official*, Caracas, May 10, 1895, *Ley de Bancos.*

ing notes was declared by the new law to belong exclusively to the nation and was not to be delegated until paper money should be at par with silver. Banks of circulation established after these conditions were restored were required to have not less than $250,000 in legal silver or gold money. The limit of issues is double the amount of the metallic reserve and the privilege cannot be granted for a longer period than seven years, but may be renewed.[1] The bank-note circulation at the end of 1894 was $26,109,557.

The two leading banks of issue in Ecuador were until recently the Bank of Ecuador and the International Bank, and their notes were maintained at par and were preferred to silver. The International Bank has recently been merged with the Bank of Commerce and Agriculture, established at Guayaquil, with a capital of 5,000,000 sucres ($2,500,000). The capital of the Bank of Ecuador, established in 1867 at Guayaquil, is 2,000,000 sucres. The banks are allowed to issue circulation to the amount of three times their coin reserve in silver. They are subject to examination by government officials, but are private corporations and the shareholders are subject to no liability beyond their investment.[2] The outstanding circulation is about 4,500,000 sucres.

Several banks of circulation exist in Bolivia and issue notes under legal regulations. The National Bank of Bolivia is located at Sucre and has a capital of 2,600,000 bolivars ($2,600,000). The Francisco Argandona Bank at Sucre, founded in 1893, has a capital of 100,000 bolivars. The Bank of Potosi is also a bank of issue. The circulation of the National Bank on June 30, 1893, was 3,532,000, bolivars and of the Francisco Argandona Bank on December 31, 1893, 393,000 bolivars. The metallic reserve in each case was about one-fourth of the circulation.[3]

There are no banks of issue in Peru, but the existing dis-

[1] *Monthly Bulletin of the Bureau of the American Republics*, February, 1895, II., 570–72.

[2] Comptroller's Report, 1895, Letter of Minister James D. Tillman, 78–9.

[3] Lévy, 279.

count banks hold government paper money in their cash reserves. This money was issued to the amount of 100,000,000 soles ($100,000,000) during the war with Chile, but has been largely retired, leaving actual transactions to be carried on in silver. The banks are permitted to establish branches and are required to pay five per cent. of their net profits as a patent tax.[1]

The National Bank of Haiti.

"The exclusive privilege of issuing bills to bearer, payable in specie on presentation," was conferred on the National Bank of Haiti by the decree of the National Assembly of April 1, 1880. The Bank was founded by French capitalists, with a capital of 10,000,000 francs ($2,000,000), and its privileges were conferred for fifty years. The charter required the coin reserve to equal at least one-third of the circulation and made the notes legal tender throughout the republic. The founders of the bank secured from the government a pledge to adopt a national currency and this was done by making the gourde the unit (equal to five French francs) and providing for gold and silver coinage at the Paris mint. The government went further and violated the privileges of the bank by issuing a national paper currency, amounting to 1,000,000 gourdes in 1884, and eventually to 6,200,000 gourdes.[2] The amount has been somewhat reduced, but has in the meantime deranged the financial system and substantially deprived the bank of the power of issuing its own notes. The bank was required by a law of September 29, 1892, to issue notes of one and two gourdes on account of the government.[3] More recently (in 1895) the National Assembly has authorized a loan for 50,000,000 francs in Europe, with which it is proposed to establish the gold standard. The National Bank manages the public debt

[1] Comptroller's Report, 1895, Letter of Richard R. Neill, Chargé d' Affaires, 94.

[2] Comptroller's Report, 1895, Letter of Minister John B. Ferris, 86.

[3] Lévy, 274.

and is exempt from taxation upon its property and notes. None of its own notes have been in circulation during the recent paper money *régime*, but the bank has done a considerable discount business through several branches. One of the branches is at Paris.

San Domingo also has a National Bank endowed with the power of note issue and in 1894 adopted the gold standard, with the United States dollar as the monetary unit.

The Banks of Central America.

The republic of Salvador contains five banks of issue, with special charters granted by the government, under the provisions of a general law. The banks are allowed to issue notes to the amount of twice their subscribed capital, but are required to hold forty per cent. of the amount of the circulation in silver coin. The Industrial Bank is required to hold a reserve of fifty per cent. against its notes, but thirty per cent. of the mortgages held may be counted as the equivalent of coin. Notes are redeemable in silver coin on demand. The five banks in operation are the International Bank of Salvador, with a capital of $3,000,000;[1] the Western Bank (*Banco Occidental*), with a capital of $2,000,000; the Salvadorean Bank (*Banco Salvadoreno*) with a capital of $3,000,000; The Industrial Bank of Salvador (*Banco Industrial del Salvador*), with a capital of $2,000,000; and the London Bank of Central America. The latter institution has only a branch in Salvador, and the proportion of the capital there employed is not absolutely fixed. The aggregate circulation of the four domestic banks is about $5,000,000.[2]

The only bank in Nicaragua is the London Bank of Central America, Limited, whose head office is in London. The bank was founded in 1888, with a nominal capital of £600,-

[1] The monetary unit in Central America is the peso, nearly equal at the old parity of gold and silver to the United States dollar, but the depreciation of silver makes its present bullion value about 50 cents. Most of the sums stated in dollars represent pesos.

[2] Comptroller's Report, 1895, Letter of Minister Lewis Baker, 99–101.

000, under the name of the Bank of Nicaragua, but only 19,567 of the 60,000 shares have been issued and only fifty per cent. has been paid up on these. The shareholders are liable only for the amount of their stock, and government officials have the right at any time to make an inspection of the books and cash of the bank. The reserve is required to be kept in silver and must equal forty per cent. of the outstanding circulation. The bank is not subject to special taxes and has the privilege of using the national railway, steamship, telegraph, and telephone lines without charge.[1] The notes of the bank are registered in the State Treasury and amounted on December 31, 1894, to £99,269. The deposits and current accounts were £89,751, and the reserve funds, including £12,000 to cover depreciation in exchange, were £23,734. The cash in hand was £154,075; bills receivable, £88,526, and loans, £68,758.

Semi-annual reports are required of banks of issue in Guatemala and the government designates experts to make periodical examinations of their books.[2] A cash reserve of fifty to sixty per cent. is usually required to be held against notes, but the charters granted have not been uniform in their requirements. The four existing banks of issue are the International Bank; the Commercial Bank of Guatemala; the Colombian Bank, with a paid-up capital of 1,630,000 pesos; and the Bank of the Occident, with a paid-up capital of 1,500,000 pesos. The International Bank had a circulation on December 31, 1894, of $2,539,747; deposits and current accounts, $3,668,270; reserve fund, $950,000; cash, $3,878,584; discounts and advances, $4,540,608. The bank also holds among its securities $382,190 in British Consols and United States four per cent. bonds.[3] The Colombian Bank had a circulation on December 31, 1894, of $434,112; the Commercial Bank, $1,220,011; and the Bank of the Occident, $1,408,029.

[1] Comptroller's Report, 1895, Letter of Minister Lewis Baker, 106.

[2] Comptroller's Report, 1895, Letter of D. Lynch Pringle, Chargé d'Affaires, 85.

[3] London *Bankers' Magazine*, May, 1895, LIX, 729.

Costa Rica has both government paper money and bank-notes in circulation. The latter are issued chiefly by the Bank of Costa Rica, which has a capital of $1,155,000 and a circulation of about $3,500,000.[1]

The Banks of European Colonies.

The banks of issue of the French colonies in America were authorized by laws of the republic passed in 1849, which put them under the supervision of the home government and under certain general regulations. These banks were authorized to issue notes no smaller than 25 francs ($5) until 1874, when the law of June 24th reduced the limit to five francs ($1). The circulation was limited to three times the metallic reserve and the liabilities were not permitted to exceed three times the capital. The French colonial banks have a common agency at Paris under the supervision of the Minister for the Colonies.[2] The Bank of Martinique and the Bank of Guadeloupe were each established in 1853, with a capital of 3,000,000 francs, while the Bank of French Guiana was founded in 1855 with a capital of 300,000 francs, which was increased in 1864 to 600,000 francs. The two older banks have loaned largely on the growing crops, which has brought them difficulties and losses in years when the crops have failed, but has contributed greatly to the convenience of the community. The Bank of Guadeloupe has a circulation of about 7,000,000 francs; the Bank of Martinique, 6,000,000 francs; and the Bank of French Guiana, 1,600,000 francs.[3] The Bank of Guadeloupe paid a dividend in 1894 of twenty-one per cent. on the nominal capital, and the management proposed to reduce the rate on loans on the crops from six to four per cent.[4]

The bank-note circulation of the British West Indies and of British Guiana is largely furnished by the Colonial Bank, with headquarters in London and fifteen branches and

[1] Lévy, 277.
[2] Courtois, 190–94.
[3] Lévy, 275.
[4] *Revue des Banques*, August, 1895, XIV., 156.

agencies. The bank was chartered by the British government in 1836 and the charter was renewed in 1856. The paid-up capital is £600,000 and the total liabilities on June 30, 1895, were £4,759,642, of which £452,672 was on account of circulation, £1,724,346 on account of deposits, and £1,794,963 for bills payable and other liabilities. The discounts were £1,771,084; bills receivable, £1,464,296, and specie £419,988.[1] Mr. Muhleman distributes the circulation among the various colonies as follows: Jamaica, $900,000; British Guiana, $300,000; Trinidad, $500,000; Barbadoes, $160,000; others, $240,000.[2] The Nassau Bank furnishes a part of the circulation in the Bahamas, based upon coin and British and United States bonds, and the British Guiana Bank provides a part of the circulation for the colony for which it is named.

The Spanish Bank of Cuba has provided the paper circulation of the largest island of the West Indies. The government utilized the bank during the insurrection several years ago for the issue of legal tender paper on government account, but this paper was withdrawn in 1893. The capital of the bank is 8,000,000 piasters ($7,400,000). Porto Rico also has a bank of issue, known as the Spanish Bank of Porto Rico. The institution was founded in 1891 and has a circulation of about 1,500,000 piasters.[3]

Dutch Guiana is provided with a circulation of about 1,000,000 florins ($400,000) by the Bank of Surinam. St. Thomas also has a bank of her own,—the Bank of St. Thomas, which issues notes in terms of dollars, running as low as $1.

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[1] London *Bankers' Magazine*, February, 1896, LXI. 293.
[2] *Monetary Systems of the World*, 113.
[3] Lévy, 276.

CHAPTER XVIII.

BANKING IN AFRICA AND THE EAST.

The Early Banking Experience of India and the Present Paper Currency—The Banking System of Japan and the Beginning of Banking in China—The Bank of Persia—The Recent Failures in Australia—The Maintenance of the Gold Standard in Java—The Colonial Banks of Great Britain, France, Spain, and Portugal.

THE banking experience of the continents of Africa and Asia and of the great islands of the Pacific offers much that is of interest to the financial student and historian, in spite of the comparatively recent creation of some of the banking systems. The influence of British capital and British models is more apparent even than in Latin America in the financial system of British India, in the great colonies of Australia and in the institutions which handle exchange with South Africa and the free ports of China. The history of the independent banking systems of the East is of peculiar interest also, because it has put to the test certain economic theories under conditions which could not have been found under the complicated and conservative financial management of European nations. One of the most interesting of these experiments is that conducted for nearly twenty years in the Island of Java, under Dutch control, where values have been maintained upon the gold standard and silver coins have been kept at parity with gold by means of the absolute limit put upon their amount, with scarcely a gold guilder in circulation and a merely nominal supply of gold in the reserves of the Bank of Java. Equally interesting promises to be the experience of China, whose

native bankers and great English companies are soon to encounter the rivalry of a bank under Russian influence, whose example is likely to invite other competitors to enter the field.

Banking in India.

The issue of circulating notes through the medium of banks was brought to an end in India in 1861, but prior to that date there was a flourishing system of banks of issue. Banking in India in the early days of European supremacy was subject to no fixed regulations. The bulk of the business was transacted for many years by the "agency houses," founded by civil and military employees who had retired from the active service of the East India Company to go into private business. They made loans to the company at a high rate during the latter part of the last century, but the rate had fallen by 1813 to six per cent. and the debt had risen to £27,000,000. Some of these houses became very powerful, but large investments in industrial establishments, which suffered many failures in 1828, 1829, and 1830, caused their downfall. The total liabilities of the six agency houses which failed from 1830 to 1834 were estimated at over £17,000,000 and one of the largest paid little more than three per cent.[1]

The era of responsible banks began after the crisis. The Bank of Bengal had been founded as early as 1809, but its charter was renewed in 1840; a charter was issued in the same year to the Bank of Bombay, with a capital of £525,000; and a charter was issued in 1842 to the Bank of Madras. The private banks had been allowed to issue notes and this was true also of the Union Bank of Calcutta, founded in 1829, and the Bank of Agra. The Bank of Bengal in 1834 refused to receive the notes of the Union Bank or any of the new concerns, and the Union Bank went down in the crisis of 1846. The Bank of Western India was founded in Bom-

[1] J. W. MacLellan, in London *Bankers' Magazine*, January, 1893, LV., 55.

bay in 1842, opened branches in Calcutta, Ceylon, and Canton, and became the Oriental Bank in 1845. This bank seems to have inaugurated the business of circuitous exchange, and encountered the unsuccessful hostility of London houses and the East India Company when it sought a royal charter in 1850.

The discovery of gold in Australia led to the projection in London of many new banks for foreign business, but it soon appeared that there was already a sufficient banking capital invested in India. The Bank of Bombay found legitimate discount business so dull that the directors endeavored to obtain a modification of their charter which would permit them to engage in exchange business in and out of India. The directors proposed, if this were granted, that the limit of note issues should be reduced from £2,000,000 to £1,000,000. The actual circulation was only £400,000, and the government refused to assent to the proposal.

The banks of the three great presidency towns had a circulation in 1860 amounting to £2,241,471, with current accounts of only £1,855,293. The circulation increased by the spring of 1861 to £3,081,599, of which £1,851,627 was issued by the Bank of Bengal, £1,006,460 by the Bank of Bombay, and £223,512 by the Bank of Madras. Each bank was required to keep in its vaults cash equal to one-fourth of all outstanding demand liabilities. No complaint had been made up to this time of the manner in which these banks conducted their business, but it was thought that a profit might be made by the government out of the issue of notes.[1] The proposition to take the power of issue away from the banks was discussed as early as April 27, 1859, in a despatch from Lord Canning, and was embodied into law in 1861. The record of the banks was less creditable after the loss of the power of note issue. The Bank of Bombay, which had been so carefully conducted for twenty years that its gross losses were computed at only £2,500, obtained a new charter in 1863, sweeping away most of the restrictions on its

[1] London *Bankers' Magazine*, April, 1893, LV., 548.

operations and permitting an increase of the capital by June, 1864, to £2,090,000. Another crash came in 1866, following the news of the failure of Overend, Gurney, and Co., in London, and the Bank of Bombay lost in three years £2,046,898, and was compelled to wind up.[1] A new Bank of Bombay was formed, and in May, 1868, the liquidator stated that £1,889,993 of the capital of the old bank had been lost. The great presidency banks are still important factors in the financial affairs of India and usually hold in their reserves from 3,000,000 to 4,000,000 rupees in government notes.[2]

The power to issue notes was withdrawn from the three banks by Act XIX., of 1861, and a paper currency established under government supervision, upon substantially the same basis as that of the issue department of the Bank of England, if entirely separated from the banking department. Some changes were made in the law in 1893, but they were principally such as were required by the suspension of the free coinage of silver. The circulation based upon securities is 80,000,000 rupees, and the interest upon these securities, which amounted to 3,452,284 for the year ending March 31, 1895, is covered into the Indian Treasury. The remainder of the circulation is represented by coin. The average gross circulation for the year ending March 31, 1863, was 44,194,385 rupees, which increased in 1869 to 101,455,327, in 1873 to 128,640,267, in 1879 to 131,905,084, in 1883 to 151,807,113, in 1889 to 164,316,288, in 1892 to 254,362,371, in 1893 to 270,995,630, in 1894 to 282,915,237, and in 1895 to 311,111,406 rupees. A considerable proportion of these notes is held in the treasury offices and the bank reserves, so that the average circulation in the hands of the public in

[1] J. W. MacLellan, in London *Bankers' Magazine*, February, 1893, LV., 223–24.

[2] The amount thus held on March 31, 1895, was 2,610,000 rupees, but the monthly average for the year was 3,740,000 rupees.—Report from Head Commissioner of Paper Currency, Calcutta, July 24, 1895. The rupee was worth about forty-eight cents in United States currency when silver was at parity with gold, but it is now worth about twenty-two cents.

1895 is calculated by the head commissioner at 185,000,000 rupees. The maximum of the year was 202,000,000 in December, 1894, and the minimum 168,400,000 in April, 1894. Redemptions, including those accomplished by the transfer of notes between treasury branches, are much more rapid than for the paper money of the United States, having reached 1,002,336,925 rupees during 1895, or more than three times the circulation. The new currency has possessed perfect security and has obviated the necessity for large transfers of silver coin, but it has lacked the element of elasticity and has restricted the expansion of banking business in India. The total liabilities of the three banks which formerly issued notes have increased in no such proportions as the liabilities of banks in other countries, and interest rates in India have averaged much higher than in countries possessing a banking currency.[1]

The suspension of free coinage in India in 1893[2] was an attempt to arrest the downward course of the silver rupee by giving it a scarcity value. The commission which considered the subject recommended that an exchange rate of one shilling, four pence (32 cents), be fixed by the offering of Council bills, sold by the government in London, at that rate. The experience of the Netherlands and the Bank of Java in thus putting an arbitrary gold value on silver token coins, and the success of Austria-Hungary and Russia in maintaining their credit paper and silver coins above the bullion value of silver, were the models of the new Indian policy. The policy was not at once successful. Rupee paper would not bring sixteen pence and the government was eventually compelled to sell it for what it would fetch. The very fact that the government succeeded in raising the value of the coined rupee somewhat above its bullion value operated to counteract the effects of this success. Silver coins began to pour out of private hoards, to be replaced (if replaced at all) by silver bars. A curious proof of this,—and a presumptive proof that the silver circulation expanded in spite

[1] London *Bankers' Magazine*, April, 1893, LV., 548.

[2] For further reference to this subject, see Chapter XXII.

of the suspension of coinage,—is afforded by the fact that coins of old coinages constituted in 1895 a considerably larger proportion of the amounts received at government treasuries than in former years. The percentage of the coins of William IV. increased from 1.47 per cent. of the total in 1894 to 1.54 in 1895; coins of 1840, first issue, from 4.0 to 4.4; second issue, from 10.99 to 11.23; and other issues up to 1882, with few exceptions, showed an increase.[1]

Banking in Japan.

Japan, after experimenting with government paper money and local banks issuing notes on the evidences of the public debt, has adopted the system of a single great bank of issue governed by regulations similar to those of the Imperial Bank of Germany. Paper money was in use in Japan for many generations, but its recent history dates from 1867. That year was marked by the overthrow of the feudal system, which had long prevailed in the Empire, and the restoration of the power of the Mikado. It was considered necessary to continue the circulation of the existing paper money in order to pay the indemnities granted to the feudal lords for the surrender of their privileges and their land taxes. A new form of paper, bearing the traditional emblems of the Empire, was adopted and acquired a more general circulation than the old.[2]

The local banks were authorized under the name of national banks by a law of 1872. The law was passed largely to prevent the fall in value of the government paper money, and the redemption of the paper was partially provided for by the issue of government stocks. The banks were required to purchase the stocks in order to issue circulating notes and were at first required to redeem their notes on demand in gold. The depreciation of silver and the excess of paper caused such a persistent demand for the

[1] Mr. F. C. Harrison, in Report from the Head Commissioner of Paper Currency, Calcutta, July 24, 1895, 39-42.

[2] G. Boissonade, *Journal des Economistes*, Sept., 1895, 410.

conversion of the notes that the banks were authorized in 1876 to redeem in government paper money. The capital of these banks was allowed to consist of any form of government stock, and the banks were required to place this stock in the custody of the government, receiving 80 per cent. of the amount in paper money. There was almost a mania for new banks between 1876 and 1879 and the number in operation at the close of the latter year was 153. Paper fell in 1877 forty per cent. in relation to silver and fifty per cent. in relation to gold, and the situation was made worse by the issue of 27,000,000 yen in government notes to pay the expenses of putting down the rebellion of 1877–78.

A new effort was made in 1878 to bring order into the disordered financial system by the suspension of further issues of paper, the issue of short-term treasury bonds bearing interest, exchangeable for government notes, and the issue of long-term bonds bearing interest at seven per cent. and payable in silver. It was announced that the redemption of a portion of these bonds annually would be accompanied by the burning of an equal quantity of paper money. These measures were completely successful. The breaking down of feudal barriers developed the domestic commerce of the country and stimulated a production which found an outlet in foreign exports and brought silver pouring into Japan in payment. The banks bought up the depreciated paper money so rapidly, in order to exchange it for bonds, that the issue of bonds had to be temporarily suspended to prevent too great a rarefication of the circulating medium. A mint was opened, specie was received at the custom-houses at its current value in paper, and in less than seven years (in 1885) paper was within five or six per cent. of par.

The new policy was promoted by the creation in 1882 of the Bank of Japan, with a capital of 20,000,000 silver yen,[1]

[1] Lévy, 235. The gold yen is worth $0.997 in United States money, but the silver yen, containing 26.956 grammes of silver nine-tenths fine, is worth only about half as much in bullion, owing to the rapid depreciation of silver in recent years. Japan is now on the silver basis.

and by the laws of 1883 and 1884, providing for the gradual retirement of the notes of the local banks and the substitution of those of the new institution. The law of 1884 prescribed the rules governing the circulation of the Bank of Japan and required that the notes be convertible into silver on demand. The bank was authorized to issue notes to the amount of 85,000,000 yen without a specie reserve and of this sum not more than 27,500,000 yen were to be issued in place of internal bank-notes cancelled after 1887. A leaf was taken from the German law in the provision that the government might permit the extension of the limit of circulation in case of need, but that the excess of circulation should be subject to a tax of five per cent. The circulation not covered by specie is required to be covered by good commercial paper or treasury bonds.[1] Circulation may be issued beyond the authorized limit without special tax when specie is held for the full amount of the excess. The bank has branches at Osaka and Shimonoseki and five sub-branches. The circulation is about 150,000,000 yen.

The Act of 1883, which regulated the retirement of the notes of the local banks, required them to surrender the privilege of note issue at the expiration of the term of twenty years for which they were originally chartered. They were required to create a fund for the redemption of their notes, from monies to be set aside annually from their profits. This fund is in the custody of the Bank of Japan, which employs it in the purchase of public stocks and cancels the notes with the proceeds of the interest on the stocks. The terms of the local banks expire between 1896 and 1899, and the government in 1894 brought in a bill providing that the banks should cease, on the expiration of their privilege, to be banks of issue and that outstanding circulation should be redeemed by the State. The bill was not finally acted on and the local banks have been making an earnest fight for an extension for ten years of the privilege of note issue. The government is still seeking the suppression of local is-

[1] Report of the Director of the Mint for 1895, 367.

sues, upon the ground that it gives the national banks an unfair advantage over the seven hundred private banks and retards the unification of the currency.[1]

Japan originally employed both gold and silver money, but was driven to the silver standard when the restoration of specie payments was attempted in 1882 and has suffered inconvenience by the great difference of exchange with gold-using countries. There has been much discussion of the currency problem and some agitation in favor of the gold standard. A commission was appointed in September, 1893, to consider the existing state of the currency and the best standard for Japanese interests. The result of their deliberations has not been harmonious and only individual reports have been submitted to the government. The theory that a high premium on specie stimulates exportations, and that its disappearance removes this stimulus, has not been directly verified in the case of Japan. Exports have steadily increased, in spite of the rise in value of the paper money; but this phenomenon is partially explained by the fact that the rise of paper in relation to silver has been neutralized by the fall of silver in relation to gold, which has left the paper money in something like its old relation to the gold standard of other countries.[2]

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[1] Letter of Jiuchi Soyeda, in *Economic Journal*, Dec., 1894, IV., 735.

[2] For another case of the failure of this theory, see Ch. XII., p. 279, under *The Banks of Greece*. M. Combes de Lestrade, in the discussion before the *Société d'Économie Politique*, at Paris, Sept. 5, 1895, declared that Russia, with a gold reserve adequate for the restoration of gold payments, allowed the paper rouble to remain below par in order to avoid a sudden arrest of exportation.—*Journal des Économistes*, Sept., 1895, 420. The effect of the silver standard in Japan, according to the observation of Mr. Soyeda, who is in the best position to know the facts, has been to raise domestic prices as well as to increase the burden of gold obligations expressed in the silver standard. He says: "The prices of exportable goods, such as rice, the chief article of food, have risen a great deal. Thus the effect of the depreciation was felt not only in the external trade, but also in the internal transactions."—*Economic Journal*, Dec., 1894, IV., 732.

Banking in China.

The bank-note circulation of China is under no legal regulation. The Chinese banks of issue are mainly at Peking and issue notes as low as ten cents, but the notes rarely circulate far from the locality. The Peking banks, however, and the discount banks in the provinces, which perform the functions of the treasury for the government, stand high in the public estimation. The issue of paper money by the government took place as far back as five hundred years before Christ, but was suspended in 1445 and has been only once resumed for a brief period.[1] No special taxes or burdens are imposed upon bankers as such, but they are expected to aid the government by loans in times of emergency. Several branches have been established in China of foreign banks, some of which issue notes in Hongkong which have acquired circulation within Chinese jurisdiction.

The greatest of the foreign banks is the Hongkong and Shanghai Banking Corporation, which was incorporated in 1864 with a capital of $2,500,000.[2] The bank began business in 1865, with several merchants of Hongkong among its directors, and has increased its capital to $10,000,000 and its note issues to $9,543,171. The report of the directors for the half-year ending June 30, 1895, showed net profits, including a small balance on hand, of $1,248,802. The sum of $492,140 of this profit was absorbed by the difference in exchange between China and the gold-using countries where the dividends are paid, but $444,444 was awarded in dividends in gold and $500,000 transferred to the reserve fund. The magnitude of the business of the bank may be judged by the fact that its liabilities were $167,128,037, including deposits of $119,804,395 and bills payable of $20,766,669. The cash in hand and in transit was $51,390,449; loans and discounts were $47,650,726, and bills receivable were $60,036,316.

Several other English and East Indian banks do business

[1] Comptroller's Report, 1895, Letter of Minister Charles Denby, 74-75.

[2] London *Bankers' Magazine*, Feb., 1893, LV., 221.

in China, but it was only in the closing months of 1895 that plans were perfected for a Russo-Chinese bank, with headquarters at St. Petersburg. The bank has been organized with a capital of 6,000,000 roubles ($4,600,000), of which more than half has been subscribed by French bankers. The capital is said to be furnished by the same syndicate which effected the issue of the Chinese loan guaranteed by the Russian government after the close of the war between China and Japan. The president of the new bank is Prince Esperukhtomsky, who has attained some prominence in Russian politics.

The Bank of Persia.

The Imperial Bank of Persia was established for thirty years by a group of English capitalists in 1889, and its head office is in London. The capital of the bank is £650,000, with authority to increase to £4,000,000, and the metallic reserve is required to be at least one-third of the amount of notes in circulation. The excess of circulation above the reserve is not allowed to exceed the amount of the capital actually paid in. The reserve may consist of gold or silver, but the charter provides that if Persia adopts the single standard of gold or silver, three-fourths of the reserve shall be held in the metal which may be adopted as the standard. The notes constitute a first lien upon the reserve and may be redeemed at the expense of reducing the reserve below the legal limit.[1] The notes, which reached £72,668 on September 20, 1895, are getting into general circulation in Persia, and branches of the bank have been established at Teheren, Ispahan, Tabiz, Meched, Shivas, Bushir, Bagdad, Basvah, and Bombay. The bank advanced £500,000 to the Persian government in 1892, for the purpose of buying back the tobacco monopoly from those who held it, and was accorded the guarantee of reimbursement from the customs duties. The dividends paid in 1895 were £35,000, notwithstanding some losses during the past few years arising from the depreciation of silver.[2] The

[1] Lévy, 236.

[2] *Revue des Banques*, Dec., 1894, XIII., 253.

aggregate assets on September 20, 1895, were £1,402,694, of which £141,986 was in cash and £799,726 in loans and discounts. The deposits were £239,164.

The Banking System of Australia.

The banking system of Australia was organized in some respects like the Scottish system prior to the crisis of 1893, but was not managed with the conservatism and good judgment which have been the characteristics of Scotch banking. The difficulties developed in the crisis of 1893, were not, however, the result of any excess of note issues, but of the error common in new countries,—excessive speculation in land and the locking up of assets in investments which did not prove immediately productive. The original Bank Act of Victoria, passed in 1864, was general in its provisions, required no independent audit of bank accounts, and imposed no definite limit upon note issues. The demand for funds for speculation in land led to heavy loans to the speculators, but some of the shrewder bankers evidently doubted their legality and secured in 1888 an important amendment of the banking law. A commission was appointed, with the avowed purpose of revising the law, and the act which resulted from their deliberations purported to impose new safeguards by requiring a paid-up capital of £125,000 for banks issuing notes and by making the notes a first charge upon the assets.[1] These reforms, however, were apparently only the cloak for the new provision that, "Any incorporated banking company may, notwithstanding anything to the contrary contained in any act in force in the Colony of Victoria relating to such banks, advance or lend money on the security of lands, houses, ships, or pledges of merchandise."

Banking in Australia had been carried to its extreme

[1] Mr. MacFie, London *Bankers' Magazine*, January, 1892, LIII., 68, 69. Notes constituted an unlimited liability in Queensland, and by the Act of 1874 in New South Wales.—London *Bankers' Magazine*, August, 1894, LVIII., 154.

limits, and millions of English and Scotch capital were attracted to the country by its rapid development and by the fact that the people were of the same blood and presumably of the same temper in business matters as the lenders. The banks of Victoria alone increased their aggregate liabilities from £19,488,512 in 1880, to £42,224,084 in 1890, while the aggregate assets increased from £23,284,822, including £3,408,961 in coin, to £60,937,955, including £6,868,328 in coin.[1] The proof of the activity and of the risks assumed in Australian banking is afforded by the proportion between available deposits and the discounts and advances made just before the crisis of 1893. The following table shows how the Australian banks loaned "up to the hilt" in comparison with the more conservative English banks:[2]

	DEPOSITS.	DISCOUNTS AND ADVANCES.
London Joint Stock Banks ..	£232,332,633	£148,942,304
English Provincial Banks....	62,272,817	46,856,402
Australian Banks.....	149,400,329	154,547,379

The proof that the evils which carried down fourteen great banks and closed several hundred branches in the spring of 1893, grew purely out of bad banking, and had substantially no connection with the note issues, is afforded by the comparatively small figures of the circulation. The banks of Victoria increased their note circulation only from £1,236,046, in 1880, to £1,543,340 in 1890, and in 1893 it was substantially the same. The chief medium of circulation in Australia was gold, and the Australian people were so well accustomed to British methods of the use of credit that the absence or presence of the power of note issue would probably have made little difference in the crisis of 1893. The inflation of credit and the crisis occurred without any great expansion of note issues, and if the habits of the people had required a concurrent expansion it would have been

[1] London *Bankers' Magazine*, April, 1892, LIII., 580.
[2] London *Bankers' Magazine*, January, 1893, LV., 46.

only an incident of the deeper causes of the crash. As M. Lévy sums up the situation : [1]

> It is worth remarking that the Australian crisis was not due to an excess of issues of bank-notes, whose figures, on the contrary, have never ceased to restrain themselves within reasonable limits, but to the large lock-ups upon mortgage advances which could not be repaid, which left the banks without the liquid resources necessary to satisfy their depositors.

The discredit thrown upon the notes of suspended banks by the crisis of 1893, and the pressure for currency which usually accompanies the disappearance of credit, led to a temporary issue of government notes in New South Wales and to some modifications of the banking law. The principal change affecting the bank-note circulation was the adoption of the provision, enacted in Victoria in 1888, making the notes of a failed bank a first charge on the assets. Bank-notes were made a legal tender except at the bank, as in the case of the notes of the Bank of England, and the amount in circulation, in excess of the coin reserve, was not permitted to exceed one-third of the capital, nor to exceed in any case £2,000,000.

The future of Australian banking is by no means free from storm-clouds. The banks adopted plans of reconstruction after the crisis of 1893, which involved the change of demand and time deposits into deferred liabilities with interest in most cases at four and a half per cent. This plan afforded a breathing spell, and the principal of these deposits does not become due in any considerable amount until 1898. The payments required in that year, are £10,605,772 ; in 1899, £10,873,620 ; in 1900, £12,258,320 ; and in 1901, £8,390,508.[2] It is already becoming a serious question how this immense mass of liability is to be met, for it is evident that, unless there is a marked change in feeling among investors in England and Scotland, the principal due there will nearly all be withdrawn. This probability presents as serious a

[1] *Mélange's Financiers*, 299.

[2] London *Bankers' Magazine*, June, 1894, LVII., 869.

problem as that which has confronted the United States during the long period of the withdrawal of foreign capital which followed the passage of the silver purchase law of 1890. It is indeed, from a mathematical standpoint, much more serious in the case of Australia, for the amount of liability to Europe is computed at £20,000,000, or at the rate of £16 per head for the Australian population.[1] If this withdrawal of capital actually takes place, it means the crippling of many Australian industries, the forced sale of land and other assets held by the banks, and the impairment of their power to pay. The prolonged payment of interest in itself on such a mass of liability means high rates for money on commercial loans and to that extent a tax upon the productive power of the colonies. The fact that these burdens are proving heavy is indicated by the second suspension, on July 17, 1895, of the City of Melbourne Bank, with liabilities of nearly £4,000,000. The bank first suspended on May 17, 1893, and reopened on July 19th following, but it was declared by the directors in a report of March 31, 1895, that the high rate of interest on deposit receipts could not be maintained. If the remaining banks meet their heavy obligations more successfully, it will be because of the great recuperative power of the colonies, the return of confidence among foreign investors, and the effect of high discount rates in attracting and holding foreign money.

The Bank of Java.

The bank-note circulation of the Dutch East Indies, of which the Island of Java forms the most important part, is furnished by the Bank of Java. The bank was founded in 1828, with a capital of 6,000,000 florins ($2,400,000),[2] but the chief interest of its history to the Western World is the success with which it has maintained the gold standard in Java since the suspension of free coinage in Holland in 1875. The situation in Java has been in many respects the same

[1] London *Bankers' Magazine*, Dec., 1894, LVIII., 741.

[2] Muhleman, 126.

as in the mother country, but the experiment is one which might have seemed more precarious because of the situation of Java in the midst of silver standard countries and the almost entire absence of gold in the reserves of the bank. Silver was for many years the legal standard of Java, but the government of Dutch India continued for a considerable time, beginning in 1818, to make the bulk of its payments in copper. This resulted in driving silver from circulation and led to the introduction of paper currency to represent the copper coins.[1] In 1875 the Bank of Java was empowered to regulate its operations according to the principles on which the Bank of Holland was working. A bill was brought forward and passed in 1877, by the Dutch Ministry, for the regulation of the currency of their Indian possessions. The principal features of this bill were the establishment of the double standard on the same basis as in Holland,—the formal suspension of the further coinage of silver.

The parity of the notes of the Bank of Java and of the silver coins is maintained through the foreign exchanges. All commercial operations with Holland or other countries in Europe are settled by bills drawn on Amsterdam or London, and the exchange has shown an extreme fluctuation never greater than five and a quarter per cent. on Amsterdam and six per cent. on London. Since 1885 the fluctuation has not been greater than three per cent. The bank rate has varied from nine per cent. for a time in 1876 to as low a rate as four per cent. in 1878 and in 1886. The mean rate in 1894 was 5.28 per cent.[2] Settlements for merchandise balances between Holland and Java are made by shipments of silver. These shipments are taken up at home by the Bank of the Netherlands against bank-notes or credits at par with gold.[3] There was an industrial crisis in Java in 1886, which was attributed in some quarters to the maintenance of the gold standard of wages and prices, but the

[1] London *Bankers' Magazine*, March, 1893, LV., 383–91.

[2] *L'Économiste Européen*, Nov. 9, 1895, VIII., 581.

[3] Letter from Mr. Van den Berg, *Report of the Indian Currency Committee*, Sen. Misc. Doc. 23, Fifty-third Cong., 1st Sess., 573.

planters adopted improved methods of production and recent years have been years of prosperity. The majority of Dutch and English observers have been disposed to regard the fixed par of exchange maintained with gold standard countries as more advantageous to the island under actual conditions of production than the possible benefits of the declining cost of production in gold obtained in silver standard countries by the comparatively slow rise in wages, rents, and raw materials. The actual gold holdings of the Bank of Java seldom exceed 6,000,000 florins ($2,400,000) [1] against a note circulation of 45,000,000 florins ($18,000,000), and gold is seldom seen in general circulation. The smaller currency consists of silver coined in Holland and the larger of the notes of the bank.

The Banks of South Africa.

The strongest banks of South Africa are mostly English institutions, with their head offices in London. The Cape Government passed an act in 1891, requiring the withdrawal of circulating notes then outstanding and the deposit of securities with the Treasurer-General to cover future issues. The only securities accepted were those of the Cape Government, which tends to justify the belief that the law was suggested by the necessity for placing the securities rather than the benefit of the banking system. The notes circulate over a wide area and no provision is made for any specific coin reserve.[2] The note issues of the great English banks are so overshadowed, however, by their discount and exchange business that the regulations on the subject are of minor importance. The development of the gold mines furnishes a metallic circulating medium of magnitude, and British methods of banking by transfers of credit are rapidly making headway into the interior of Africa. The unusual stimulus given to business in South Africa during the past few years by the great gold discoveries has afforded the

[1] Lévy, 297.

[2] London *Bankers' Magazine*, Jan., 1892, LIII., 100–101.

banks large profits, and has led in one case to an increase of capital and in another case to a proposed increase of note issues; but the latter increase will carry the note issues of the bank hardly above ten per cent. of the aggregate liabilities.

The Standard Bank of South Africa is the largest of the English banks, with a paid-up capital of £1,000,000. The note circulation on June 30, 1895, was £730,389, but the aggregate liabilities were £15,873,509. It was announced at the annual meeting, on October 8, 1895, that taking the five items on the other side, of cash, deposits with bankers, native gold investments, and bills bought, they held in liquid assets and readily available securities £10,673,430, or more than eighty-four per cent. of the indebtedness. The dividend and bonus paid for the year was sixteen per cent.[1] The Bank of Africa, which had liabilities on June 30, 1895, of £4,683,249, authorized an increase of its paid-up capital, at the annual meeting on September 25, 1895, from £250,000 to £525,000. The note circulation on June 30, 1895, was £151,495, and the cash held was £1,026,919.[2] The bank which has proposed an increase of note issues is the African Banking Corporation, which has a paid-up capital of £297,645. The total liabilities on September 30, 1895, were £3,843,147, but the circulation was only £33,870, with a cash reserve of £1,382,037, and the proposed increase in circulation is only £250,000, for the purpose of extending branches in Rhodesia, Natal, and the Transvaal.[3]

The National Bank of the South African Republic, situated at Pretoria, was founded in 1891, with a capital of £502,000. The bank showed profits in 1893 of £42,000, but the larger portion (£35,000) was transferred to a special reserve fund, to cover possible losses on securities reverting to the bank by the default of borrowers upon them.[4] The circulation is about £130,000 and is covered many times by

[1] London *Bankers' Magazine*, Nov., 1895, LX., 656.
[2] London *Bankers' Magazine*, Nov., 1895, LX., 637.
[3] London *Bankers' Magazine*, Nov., 1895, LX., 661.
[4] *Révue des Banques*, June, 1894, XIII., 128.

the coin reserve. The aggregate liabilities in 1894 were £2,281,472.

The Orange River Free State has a national bank with a capital of £100,000 and a circulation of less than £400,000, against a cash reserve of about £600,000.[1]

The Colonial Banks of European Countries.

The bank-note circulation of the French colonies in Asia is controlled by the Bank of Indo-China, which was established by the decree of January 21, 1875, subsequently modified by the decree of February 20, 1888. The capital of the bank is 12,000,000 francs ($2,400,000), and its privilege runs until January 21, 1905. It is authorized to do the business of a bank of issue, loans, and discounts for Cochin-China, French India, and New Caledonia, as well as for the protectorate of Cambodia, Annam, and Tonkin. There are branches in China and Japan, at Pondicherry in India, and in various other parts of Asia and Oceanica. The note issues are not permitted to exceed three times the metallic reserve and the liabilities on account of notes, deposit accounts, and other debts are not permitted to exceed three times the capital and reserve, unless the excess is fully covered by coin. The bank is obliged to deal in several different forms of money to meet the tastes of its various customers. Mexican dollars have been coined at the Paris mint, rupees are used at Pondicherry, and francs are used in keeping the accounts of the bank and in parts of its territory.[2] The larger proportion of the money issued through the bank has consisted of piasters, which correspond to the trade dollar of 420 grains, formerly issued by the United States, but efforts are being made to put the French franc into circulation as the monetary unit. The note circulation of the bank of Indo-China at the close of 1894 was 22,482,000 francs ($4,400,000), the cash reserve was 9,080,000 francs,

[1] Lévy, 246.

[2] Lévy, 231.

the deposits were 8,577,000 francs and the loans were 19,415,000 francs.[1]

The circulation of Algeria is furnished by the Bank of Algeria, which was given the exclusive privilege of note issue by the Act of August 4, 1851. The privilege was originally granted for twenty years, but was extended by various decrees until November 1, 1897. The capital of the bank was originally 3,000,000 francs, but is now 20,000,000 francs. The notes are legal tender at public depositaries and by individuals. The cash reserve is not permitted to be less than one-third of the amount of the notes and current accounts. The capital of the bank is invested in French public securities and the director is appointed by the President of the Republic upon the nomination of the Minister of Finance. A limit of circulation, to the amount of 18,000,000 francs, was fixed by the law of August 12, 1870, which suspended specie payments for Algeria as well as for the Bank of France, but the maximum circulation was three times increased until it was fixed by the law of March 26, 1872, at 48,000,000 francs. The resumption of specie payments was followed by the law of April 3, 1880, which abolished a fixed limit and left the circulation to be governed by the law of 1851.[2]

The Bank of Senegal began business August 4, 1855, under the general conditions of the law of April 30, 1849. The cash reserve is required to equal one-third of the notes in circulation, and the circulation, the current accounts, and other liabilities are not allowed to exceed three times the capital, unless the additional liability is represented in full by a corresponding increase of the metallic reserve. The bank is subject to the supervision of the Minister for the Colonies at Paris, like the colonial banks of Latin America, and conducts business through the same Parisian agency. The capital of the Bank of Senegal is 600,000 francs and the circulation is about 1,000,000 francs, with a metallic reserve

[1] Muhleman, 97.
[2] Courtois, 197.

of 750,000 francs. The aggregate operations in 1894 were 5,093,594 francs in loans and discounts and 6,996,075 francs in exchange operations, and the dividend paid was thirteen and a half per cent.[1]

The Bank of Réunion was founded July 4, 1853, and has a capital of 4,000,000 francs. The circulation is about 8,000,000 francs and is governed by the conditions of the French law of 1849. The Bank of Réunion showed a considerable loss in loans and discounts during 1894, but an increase in exchange operations. The losses of the bank were chiefly through a banking company which was one of its principal clients, and a subsidy of 8,000,000 francs was voted by the local government in order to save an institution considered indispensable to the existence of the colony. The metallic reserve fell 487,606 francs below the legal reguirements on June 30, 1894, and the bank has been again threatened with difficulties by the acute competition in France of the tapioca crop of Singapore, which enjoys the advantage of the difference in exchange between silver and gold using countries. Réunion is on the gold basis, while Singapore pays wages and other costs of production in silver and sells in gold markets at an enhanced profit. The bankers and planters of Réunion have recently asked the imposition of a heavy tariff in France on tapioca from other than French colonies, in order to hold the French market.[2]

The Portuguese colonies in Africa are provided with circulation by the Ultramarine Bank (*Banco Ultramarino*), which has its principal offices at Lisbon and was founded in 1864. The notes of the bank circulate at Cape Verd and in Portuguese Guinea. The Philippine Islands are served by the Spanish Bank of the Philippines (*Banco Espagnol Filipino*), with a capital of 600,000 pesetas and a circulation of about twice this amount.[3]

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[1] *Revue des Banques*, Aug., 1895, XIV., 136.
[2] *L'Économiste Européen*, Nov. 9, 1895, VIII., 580.
[3] Lévy, 287.

CHAPTER XIX.

CRISES AND THEIR CAUSES.

The Recurrence of Crises at Regular Intervals Due to General Causes —The Operation of a Credit Cycle upon Production, upon Loanable Capital, and upon the Accounts of the Banks—The Effect of Overproduction and of Machinery—Influence of a Crisis upon the Distribution of Wealth—Bank-Notes a Small Factor in Inflation of Credit.

AN economic crisis is the sudden arrest of commercial activity and the collapse of credit. Such crises have been an important phase of modern industrial development and have been essentially periodic in their recurrence.[1] Particular events in nature and political history have been sought as the explanation of economic crises, and these events have not been without their influence; but the conditions which have produced crises have been of a more universal character and are intimately interwoven with the structure of modern credit and the speculative tendencies of the human mind. A period of speculation and expansion,

[1] A distinction is sometimes made between financial and commercial crises, according to their particular phenomena or the causes which bring them about. A panic often occurs in the money market or on the stock exchange, as the result of a great failure, a political event, or a mere rumor. Such events, where they produce no effect upon the general movement of affairs, may be described as financial or purely monetary crises, if they are worth dignifying with any special designation; but those here treated are those which affect the whole economic development of the community, because they are the result of a long train of events and usually involve elements both financial and commercial.

followed by a sudden arrest of the expansive movement and a collapse of credit, complete a credit cycle and produce the conditions for the beginning of a new cycle within substantially the same orbit as the old. In tracing the movements of credit through a completed cycle, it is proper to begin during the period of quiescence and distrust which follows a crisis. At such times the capital which has survived the crisis accumulates in the banks, where it lies largely idle, partly because the arrest of business activity has curtailed the demand for capital and partly because safety is preferred to profit, for the time being, by the owners of capital.

The seeds of a new crisis are sown in three ways,—in the production of merchandise, in the excessive consumption which apparent prosperity brings, and in the effect of production and consumption upon loanable capital. The effect of reviving industry upon production is a rise of prices. The markets have gradually become barren of commodities as the result of the arrest of production following the panic. The demand, which was less than the supply, suddenly confronts a supply which is insufficient. Prices rise, mill-wheels and factories are set in motion, the demand for the essentials of life increases the purchasing power of their producers, and their demand sets in motion again the production of luxuries or less essential articles. The movement of revival is thus diffused by degrees through the whole community. Prices pursue a constantly ascending scale, as the demand from all quarters increases, and the restoration of business prosperity becomes an accomplished and completed fact. The effect of the upward movement in stimulating a speculative advance in prices is well described by Mr. John Stuart Mill in his chapter on "The Influence of Credit on Prices." He says:

> The inclination of the mercantile public to increase their demand for commodities by making use of all or much of their credit as a purchasing power, depends on their expectation of profit. When there is a general impression that the price of some commodity is likely to rise, from an extra demand, a short crop, obstructions to importation, or any other cause, there is a disposition among dealers

to increase their stocks, in order to profit by the expected rise. This disposition tends in itself to produce the effect which it looks forward to, a rise of price: and if the rise is considerable and progressive, other speculators are attracted, who, so long as the price has not begun to fall, are willing to believe that it will continue rising. These, by further purchases, produce a further advance: and thus a rise of price for which there were originally some rational grounds, is often heightened by merely speculative purchases, until it greatly exceeds what the original grounds will justify. After a time this begins to be perceived; the price ceases to rise, and the holders, thinking it time to realize their gains, are anxious to sell. Then the price begins to decline: the holders rush into market to avoid a still greater loss, and, few being willing to buy in a falling market, the price falls much more suddenly than it rose.[1]

This revival of industry gradually affects the character of consumption as well as of production. Those who practiced economies, and lived closely within their incomes through the period of depression, begin planning their mode of living upon the basis of future profits as well as within their actually increased earnings. Houses are planned, carriages and servants are employed, and other luxuries are used, which would not be used but for the belief in constantly growing earnings and profits. People live beyond their incomes and consume the product of other people's labor and of their own savings. It is this which makes a community so poor when the cycle has run its course. There is no better established law of political economy than that the means of employing labor in the future are the product of past savings. When these savings have been dissipated in luxuriant living, there is no adequate capital left to employ labor or to continue the old scale of expenditure. As Prof. Bonamy Price remarks, "If all England took to eating and drinking up and consuming everything in the land in one year, the abundance and luxury and enjoyment of riches would be what the world had never seen."[2] But it could not last. Those who have been spending more capital than they have been really earning go into bankruptcy and

[1] *Principles of Political Economy*, B. III., Ch. xii., Sec. 3.
[2] *Currency and Banking*, 147.

the loss falls upon those who have advanced them their own capital in the form of horses, carriages, wines, woollens, silks, and houses. The suspension of the production which supplied these people with luxuries would in itself diminish the present demand for labor and change the course of industrial development. When the mere cessation of demand is accompanied by inability to pay for what has been consumed, the situation becomes even worse. The business community wake up to the fact that they have consumed the savings of past years, that production to meet this fictitious demand must cease, and that even a normal and healthful demand must be curtailed while society is repairing its shattered forces.

These influences at work in the merchandise markets cannot fail to have an influence upon the market for capital. Capital is idle and redundant during the period of liquidation following a crisis. Those who have it are afraid to invest, and those who usually employ it are indisposed to enter the market as borrowers. When this feeling has partially subsided, capital can be obtained at low rates, so long as the security is good, because it is so plentiful. Low rates and ample supplies of capital tempt borrowers, and industries develop into activity and reduce the idle accumulation of capital in the banks. The demand increases the rate of interest, at the same time that the demand for commodities increases their price and makes more money necessary to carry on a given business. The mere advance in prices, as pointed out by Mr. Mill, tempts to increased production, to new investments and increased speculation, and every such step increases the demand for capital at the same time that it diminishes the supply. The time comes when exports diminish because of their high prices as compared with those of the same goods in other countries; and then gold, —the only money which can be used in international exchanges,—begins to go abroad, instead of commodities, in payment for commodities imported.

The withdrawal of gold from the bank reserves and its export abroad is usually the most striking visible sign that

business is upon the eve of a crisis. When goods can no longer be sold as rapidly as they are produced,—partly because domestic purchasers can no longer pay the enhanced prices and partly because foreign purchasers can buy similar goods elsewhere at less prices,—the manufacturers and merchants are no longer able to meet their obligations at the banks at maturity. They apply for extensions and continuances and impose a constantly increasing strain upon the banking reserves of the banks. When the banks are no longer able to lend with the same freedom as before, their weaker customers default in their obligations, and the panic begins. The dream of rapidly acquired riches, of constantly rising prices, of a perpetual advance in the stock market and of extravagant profits, is suddenly brought to an end and merchants lose their illusions and look about to discover their real situation. They often find that the rise in the price of their raw materials has kept pace with that of their products, that their seeming profits have been calculated by over-discounting of the future, and that they have a great stock of goods on their hands which cannot be sold at the cost of production.

The effects of a crisis upon the accounts of a bank follow so uniform a rule that the history of crises might easily be traced, by one who understands their operation, by the fluctuations in the bank returns. The period of speculation and ascending prices is marked by a steadily widening separation between the amount of the cash reserves and of the loans and discounts. The cash falls while the loans rise. The fall in the cash is partly due to the steadily growing domestic demand for currency and credit, to meet which the cash is put in circulation ; but the decline is sharply accentuated, after speculation reaches the danger-point, by the demand for cash for settling foreign balances which have ceased to be settled in merchandise. The changed condition of the bank's accounts up to this point is brought about by the gradual operation of the expansion of credit and the rise of prices. The discovery that the danger-point has been reached, and that cash and discounts are too far apart, usu-

ally comes suddenly, as the result of heavy withdrawals of specie for export. Then begins the panic, which becomes more or less acute according to the circumstances of the case and the extent to which credit has been overstrained. The demands for loans and advances increase, while the decline of the cash reserve becomes so rapid as to compel a prudent bank to raise the rate of discount. The effect of the increase in the discount rate is to diminish the demand for credit from those who can do without it, while it attracts capital from abroad or,—what is substantially the same thing,—induces foreign creditors to suspend the withdrawal of their credits by the attraction of their higher earning power.

The moment the acute danger is over and the rush for currency has ceased, a radical change comes over the accounts of the bank as the result of the arrest in the activity of affairs. The demand for credit declines to a minimum, resulting in the reduction of loans and discounts, while the diminished demand for currency sends it back to the solvent banks and results in the rapid piling up of specie in their reserves. These movements are the result of inevitable financial laws, which seem to act with automatic precision at the various stages of a credit cycle. The movement of deposits varies somewhat, according to the real pressure of the crisis and the banking rules by which deposits are regulated. The general tendency of the real deposits,—those which are not merely transfers of credit by the bank to its customers on account of loans,—is to follow the cash reserve. They diminish when the demand for currency is most acute and begin to accumulate again when the crisis is over. Their recovery is usually less rapid than that of the cash reserves and is comparatively slow where real losses have been heavy and the wealth has disappeared which made deposits possible. The movement to withdraw deposits because of distrust of solvency of the banks is more abnormal and has been reduced in recent crises to a comparatively small factor. Such withdrawals, without commercial reasons, greatly cripple the powers of a bank to assist those who need assistance and have been among the most serious dan-

gers of financial crises, where banking was not regulated by sound laws and among peoples where its methods were not well understood.

The intensity of the demand for credit after the arrest of inflation and of the rise of prices is usually in an inverse ratio to the possibility of getting it. The demand of the moment is for cash, or what represents cash in its general acceptability in the discharge of obligations. So long as banks are solvent, and their solvency is generally credited, bank-notes fulfil this demand as absolutely as gold. This has been proved repeatedly in the case of the Bank of England and of the Scotch banks, and was proved in the case of the banks of the United States during the crisis of 1893. If currency is hoarded under a solvent banking system, it is because the amount is believed to be limited and those who hoard it fear that they may not be able to obtain the share which they need at the moment when it may be demanded. An elastic limit of note issue is a powerful weapon for restoring financial confidence on such occasions. It was the existence of a practically rigid limit in England in 1847, 1857, and 1866, and in the United States in 1893, which led to the pressure for currency and the tendency to hoard it. The removal of the rigid limit,—by means of the suspension of the Bank Act in England and by the issue of Clearing House certificates and certified checks in the United States, —did much to restore healthful conditions to the financial organism.

The expansive theory, at it is called by Professor MacLeod, has been too often tested during the past half century against the restrictive theory to leave any doubt as to the wisdom of the former. The expansive theory involves loans in times of panic up to the utmost limit, upon good security, which the resources of the bank permit, in order to meet the emergency of the moment. A solvent bank need have no fear in a crisis, if it has the power to issue notes which command the public confidence, that it will not find its specie reserves fully restored after the acute stage of the crisis is over. The power of note issue may be employed to the

extreme limit, so long as general business itself and the business of the bank are substantially sound. The restrictive theory assumes the necessity of bringing everything at once to a metallic basis. It is supposed to have the effect upon the congested financial body of a healthy purging; and the principle might be defensible, if it were not for the hardships which it causes to persons who have not carried the inflation of their business to an extreme point and who are simply embarrassed by the unusual clamor of the moment for cash. One of the duties of the banks is to sustain such people until the panic is over and the operations of credit return to their normal channels. In the language of Mr. Bagehot, in criticising the course of the Bank of England :[1]

> What is wanted and what is necessary to stop a panic, is to diffuse the impression that though money may be dear, still money is to be had; if people could be really convinced that they could have money if they wait a day or two, and that utter ruin is not coming, most likely they would cease to run in such a mad way for money.

The regularity with which production and the absorption of capital proceed, from the period of quiescence after a crisis to the point of excessive expansion, followed by a sudden check, a crisis and a new period of quiescence, justifies the theory that crises are substantially periodic in their recurrence. The seeking of special causes may be of value to enable the business community to guard against the repetition of old mistakes, but the belief that conditions can be produced which will put an end to the regular cycle of credit contraction and expansion has not been justified by any theory of banking, of trade, or of public finance which has yet been tested. The field for making such tests is limited to a few great commercial nations, because the perturbations in nations where production is more limited and credit more restrained are of a different character, often influenced more by local than general causes, and afford little instruction for the great trading nations. These great nations, moreover, are governed by the most divergent

[1] *Lombard Street*, Works, V., 45.

policies in respect to tariffs, monetary standards, banking methods, and the intervention of the State in private affairs; yet the phenomena of recurring cycles of expansion and contraction, of exaltation and of depression, are in many respects the same.[1] In the language of M. Juglar, "Wars, revolutions, tariff changes, loans, variations of fashion, new pathways opened to commerce are still accused" as the cause of crises.[2] One of these events often comes to precipitate the panic at a particular moment, like the match which causes the explosion when the powder train is fully laid. These special causes, however, grow less easy of definition and isolation as the structure of commerce and credit grows more complex and the industries of every producing nation reach out to new and diversified fields.

The salient feature of nearly every crisis has been the sinking of capital in unproductive enterprises. These enterprises have usually been in new fields, whose limitations have not been accurately measured by investors or even by capitalists of presumed judgment and experience. The opening of such a field has been followed by a rush in that direction, which has quickly exhausted all its possibilities and resulted in overproduction and the loss of the capital invested. New discoveries and the opening of new continents have contributed greatly to these mistakes during the modern commercial age. One of the earliest of these phenomena, which took place under modern conditions, was the sinking of capital in canals in England in the middle of the

[1] The argument is not without plausibility that the protective tariff policy contributes to the frequency and severity of crises, by the artificial stimulus which it gives to favored industries,—inviting great investments of capital in these directions, which result in overproduction and subsequent stagnation. The effect of such a policy would seem to be to give a jerky development to industry, causing successive periods of extreme activity and exhaustive reaction, like the effect of powerful stimulants upon the physical body. The protectionists are able to answer that Great Britain, the chief free-trade country, has suffered panics as acute as those of any other nation, if they have not affected equally her permanent prosperity.

[2] *Des Crises Commerciales*, 5.

eighteenth century. It was the beginning of the wonderful new birth of the world out of the grave of feudalism into the modern age of machinery, steam, and electricity. The sinking of capital in canals was followed by changes from hand to machine labor, which threw laborers out of employment and destroyed the value of their simple tools; by loans to farmers for enclosure and irrigation; by immense subsidies by England to European nations; and by fifteen years of the continuous waste of war. When the investing public of Great Britain and Europe had recovered from the losses consequent on these events, they permitted millions to be swept away in the crisis of 1825 by foolish investments in Latin-American securities; in 1837, by loans in the United States; in 1847, by the failure of the cotton crops; in 1857, by railway speculation; in 1866, by the effects of the American war and useless investments in cotton mills and ships; in 1873, by railway building in the American wilderness; and in 1890, by a new fever of investment in South America.

The overproduction of commodities by means of machinery has been one of the recent forms of the sinking of capital. The use of machinery has immensely increased the productive power of the world and added to the sum of comforts to be distributed among mankind. But this power of production has been carried to such a point that it has in many cases outrun the effective demand of the community.[1] Overproduction in a broad sense is hardly within the power of the entire producing mechanism of mankind. The world

[1] Prof. Lexis of Gottingen points out that overproduction is now due in many cases to the development of the industrial capacity of establishments far beyond any concurrent market demand and to their long continued operation when they have ceased to pay dividends. Abstract political economy of the old school taught that when prices no longer equalled the cost of production and a fair profit, production would be diminished or suspended; but the system of joint stock companies enables many to remain in operation for years without paying dividends, where an individual employer would close, and even the latter is often tempted to continue an unprofitable production upon the theory that he thereby avoids the "deterioration of the plant."—Wells, 73.

is not too rich in the products of human labor, but is still too poor. But overproduction for all practical purposes is production beyond the effective demand of those who have the means and habit of using, and the capital employed in the production of goods which are not consumed is more hopelessly sunk than if devoted to railways or public works; for railways and public works may prove of value in the future, even if their production has outrun the necessities of the present.[1]

One of the striking effects of a commercial crisis under modern conditions is its influence upon the distribution of wealth. Accumulated capital suffers much more than productive industry and the result is to transfer the interest on such accumulations and a part of the principal to labor. Those laborers who continue to earn their customary wages, including those who earn professional salaries as well as those who labor with their hands, are benefited materially in a period of low prices, because of the greatly increased purchasing power of their earnings. Even laborers who are thrown out of employment cannot suffer any such loss in a modern civilized state as is suffered by capital; for, if they are without savings, they derive the means of subsistence from public charity, contributed by taxation upon the accumulated earnings of capital. Only so far as their degree of comfort under such conditions differs from that when they are wage earners do they suffer an actual material loss, whatever may be the social evils of their situation.

But the effect of a crisis upon the distribution of wealth is more profound than the mere losses which it occasions during the period of acute depression. Such a crisis is the result of overproduction and is followed by the accumulation of idle capital in the banks and public depositaries. Every crisis of modern times has witnessed a greater ac-

[1] Prof. Paul Leroy-Beaulieu points out that a railway constitutes an actual economic benefit to the community, even though it fails to pay operating expenses, if the economy in transportation which results from its operation as compared with pre-existing means of transportation is sufficient to pay the interest on the capital invested.—*La Science des Finances*, II., 216, note.

cumulation of idle capital than those which have preceded, and the result has been keenly felt in recent years in the decline in the rate of interest. A given capital which earned six per cent. a decade or two ago now earns but three or four per cent. and double the accumulation is required to render the same return. Every crisis corrects the tendency to the undue earnings of accumulated capital by arresting the advance in prices, reducing the value of manufacturing and railway plants and of the securities which represent them, and in many cases compelling the readjustment of nominal capital upon a reduced basis. Capital is often deprived absolutely of earning capacity for several years following a crisis. This implies that if production continues, the proceeds are distributed without charge beyond the wages of labor among the consumers of the community. An industrial enterprise which continues to operate without profit or at a loss during a period of depression transfers all its benefits, therefore, to the wage earners, and their wealth is enhanced at the expense of the owners of inherited or accumulated capital.[1]

The argument is sometimes made that issues of paper currency pave the way for crises because they pile up a vast

[1] This theory has been more boldly worked out by Bastiat in his *Harmonies Économiques*, and recently by M. Eudore Pirmez in his *La Crise: Situation Économique de la Belgique*, 1884, who declares that "In the measure that capital increases, the absolute share of the capitalist in the total product is augmented and his relative part diminished. The laborer, on the contrary, sees his share augment in both senses." A striking illustration of the shrinkage of the earnings of capital is afforded by a table printed by M. Hector Denis, showing the dividends of corporations in Belgium from 1870 to 1890. The maximum was attained in 1871, when corporate earnings were 77,332,342 francs. The figures shrunk in 1877 to 38,837,320 francs, after which they gradually recovered until 1883, when they were 61,860,805 francs. There were some losses in succeeding years, and the amount in 1885 was 48,721,046 francs, but the total in 1890 had risen again to 71,875,225 francs. It is obvious that a range of fluctuations representing fifty per cent. of the maximum is greater than could be matched for the aggregate earnings of labor. *La Dépression Économique et Sociale*, 61–79.

credit structure on a slender basis of coin. While this conception may have some incidental truth, the fundamental idea upon which it is usually based is wrong. A bank-note is secured by the substantial assets of the bank, which are chiefly bills of exchange representing commodities. It does not matter, so long as the bills are genuine, that the same merchandise may have been the subject of several transactions and of several bills, for the maker or endorser has in each case substantial means to cover his obligations if he is doing a prudent business. Credit may be overstrained, fictitious bills may be drawn, and losses may result, but such losses are not often due to the issue of bank-notes. A man may strain his credit by too many verbal promises to pay bags of gold, where a purely metallic currency is used, just as he may strain it by putting those promises in the form of negotiable paper. He may strain it even more by book credits and abuse of the confidence of capitalists than he can ever do, under modern conditions, by obtaining notes from a banker. Nothing but the brushing away of all forms of credit, and return to barter and the hoarding of vast piles of gold, would prevent any possible abuse of credit; and that would be the destruction of modern commerce, with all the increase in productive power and the distribution of the products of that power which it has brought to the human race.

The conception that every transaction in which coin does not pass is a credit transaction ignores the essential fact that the business community is trading in commodities and not in the precious metals. The advocates of a larger metallic circulation have a favorite metaphor by which they picture "the vast structure of credit" as an inverted pyramid, supported in unstable equilibrium upon a golden apex. A better image than that of the inverted pyramid would be that of the railway or canal, which by a single route permits the happy interchange of all commodities.[1]

[1] "Currency, therefore, is not capital, any more than ships are freight; it is only a labor-saving machine for making easy transfers." Sumner, *History of American Currency*, 171.

Proper facilities for transportation do not require a car for every car-load of wheat which exists nor a canal broad enough for all vessels to pass abreast. The possibility of having the car when it is needed, the promise of the use of the canal for a brief time, serve every purpose; and no one thinks of charging that the transportation system is "a vast structure of credit" resting upon a few real cars or upon abnormally narrow tracks.

CHAPTER XX.

THE EARLY CRISES OF THE CENTURY.

The Periodicity of Crises up to 1793—The Use of Accommodation Bills in the Crisis of 1782—The Effects of the Napoleonic Wars and the Crisis of 1810—The Speculative Mania of 1825—The Specie Circular and the Bank War in the United States—The Railway Development and the Crisis of 1847.

THE development of existing methods of commerce and of credit belongs essentially to the period of the last century and a half. Great commercial transactions were carried on before that time, but they were carried on by other banking methods than those of the modern age. The world was not linked, as it is to-day, in all its parts, by a community of commercial operations and by houses of international banking credit. Such economic crises as occurred were local in their effects and were produced, much more directly and more often than those of to-day, by political events. Their chief interest, therefore, is in demonstrating the essentially periodic character of such convulsions wherever commerce has attained anything like its modern development. Professor Jevons finds some evidence of a stock-jobbing mania as far back as 1682 and others in 1711, 1721, 1731, 1763, 1772–73, and 1783, with evidence of periods of high prices in 1742 and 1752. Complaints of stock jobbing and "bubbling" were so pronounced that acts were passed by Parliament in 1710 and 1711, and again in 1733, with the result, according to Defoe, that "a happy stop was put to this spreading mischief." [1]

[1] Jevons, *Investigations in Currency and Finance*, 210–211.

The first serious credit crisis of which authentic details exist was that of 1763, when the inflated bubble blown by the Seven Years' War was pricked by the coming of peace. This crisis is of peculiar interest, because it was most severe at Amsterdam and Hamburg, where no paper currency was employed except the "bank money" issued against deposits of coin by the Bank of Amsterdam and the Bank of Hamburg. The next great crisis,—that of 1772,—fell upon England and Scotland in the midst of a period of remarkable industrial and inventive activity. The first act for the building of a canal in England was passed in 1755, and the next twenty-five years witnessed the construction of a network of canals more extensive than those of any other country except Holland. Brindley completed the canal from Worsley to Manchester in 1762 and Arkwright and Watt were at the same time developing their wonderful mechanical inventions.

The practice of drawing accommodation bills seems to have come into use in Scotland for the first time just before this crisis, although there is evidence that it had been practised earlier in England. A newspaper of the time contained a letter stating that "Banking companies had appeared in almost every corner of the Kingdom, and bills of exchange had been multiplied by a new method called Swivelling, without any solid transactions."[1] Adam Smith alludes to "the well-known shift of drawing and redrawing," and says that "The practice of raising money in this manner had been long known in England, and during the course of the late war, when the high profits of trade afforded a great temptation to overtrading, is said to have been carried on to a very great extent."[2] Professor MacLeod declares the system of accommodation bills to be "the curse and bane of commerce," and expresses the opinion that "it has been the great cause of those frightful commercial crises which seem periodically to recur." The English courts have decided, however, that a bill given for a consideration is a good bill

[1] *Public Advertiser*, July 8, 1772, quoted by MacLeod, II., 215.
[2] *Wealth of Nations*, Book II., Ch. ii.

and that such consideration exists when such bills are mutually interchanged. This makes it difficult to legislate against accommodation bills, even if it were desirable, without destroying banking transactions, which are based upon a similar interchange of credits.[1]

The crisis of 1783 is notable for having had an international character, in affecting the *Caisse d'Escompte* in Paris as well as the British banks, and for the enlightened policy of sustaining credit adopted by the Bank of England. A policy of rigid contraction was at first followed by the directors, but as soon as this policy had turned the flow of bullion towards England they came boldly to the assistance of the government and expanded their discounts to solvent houses. A different policy was pursued in the crisis of 1793 and it was the government, instead of the bank, which came to the relief of credit. Everything was ripe in England in 1792 for the explosion of a crisis when the disturbances in France and the declaration of war by the National Convention applied the torch.[2] A large failure occurred in London on February 15, 1793, and the panic spread throughout England, causing the failure of over one hundred of the country banks and frightening the Bank of England into the reduction of its discounts.[3] The pressure for money suggested to Sir John Sinclair a return to Montague's device in 1697 of issuing Exchequer bills to solvent merchants. A committee was appointed by the House of Commons, which promptly re-

[1] MacLeod, *Theory and Practice of Banking*, I., 359–68.

[2] M. Juglar lays stress upon the fact that this crisis was a typical commercial crisis, due to economic conditions, and was not essentially hastened by the declaration of war, for unfavorable exchanges and exports of specie had already set in twelve months before hostilities. France suffered a severe crop failure in 1789, but this did not arrest the expansion of credit and of commercial operations until the period of ten years from the preceding crisis of 1783.—*Des Crises Commerciales*, 302.

[3] Country merchants and bankers were permitted under then existing laws to issue optional notes, payable in the country or in London, and it is stated that out of 279 country bankers issuing notes 204 issued these optional notes.—Levi, 69.

ported in favor of the issue of £5,000,000 in such bills under the direction of a board of commissioners. The bill was passed after some opposition and afforded almost instant relief. Applications for £2,202,000, made by 238 persons or firms, were granted and only forty-nine applications were definitely rejected. Only two of the parties assisted became bankrupt, much of the money was repaid before it was due, and the government obtained a clear profit, above all incidental expenses, of £4348.

The period from the crisis of 1793 to the close of the Napoleonic wars in 1815 was marked by several spasms of panic in the markets of Great Britain and the Continent, but these convulsions were so directly due to political events that they lose much of the regular character of commercial phenomena. The period of expanding credit was interrupted in England by the suspension of specie payments in 1797, and was again cut short in 1803, after the upward movement had been resumed, by the rupture of the Peace of Amiens. France witnessed a collapse of credit soon after the rupture of the Peace, which brought Napoleon back from Austerlitz to reorganize the Bank of France.[1] The speculative opportunities of the long war left their impress upon the trade of Europe and the United States for many years, and the incidents of the trade drove the United States into war with Great Britain.

The Crisis of 1810.

The publication of the Berlin decree of Napoleon on November 21, 1806, shutting British commerce out of Europe, was one of a series of events which led to the wildest speculation in raw materials and steadily advanced their prices. The products of the countries of the East rose to double or treble their usual figures, and the French occupation of Spain quadrupled the price of Spanish wool. France was supreme in Italy, which affected the value of silk, and she attempted to dictate a policy of exclusion against Great Britain to Russia and Sweden. These efforts of the French

[1] *Vide* p. 52.

Emperor were far from effective in stifling commerce, but they gave it the character of a speculation and enhanced its profits when it was successful. The imports of the United Kingdom increased from £28,561,270 in 1805 to £39,301,-612 in 1810 and the exports increased in the same period from £31,064,492 to £43,568,757. England lost trade in the United States by her retaliatory decrees against Napoleon, which drove American products to France, but British goods penetrated through Napoleon's paper blockade at Embden and Hamburg, and the corrupt French officials grew rich as the price of certifying that these goods were the product of Prussian factories.[1] The country banks of England increased under the stimulus of speculation from 270 in 1797 to 600 in 1808, and 721 in 1810. The Bank of England, in the meantime, increased its discounts from £9,100,-000 in 1804 to £16,400,000 in 1809, and £21,400,000 in 1810. The circulation of the Bank of England rose from £16,400,-000 in 1801 to £24,200,000 in 1810, but the increase was trifling up to 1809 and was the consequence rather than the cause of the great increase in prices due to speculation.

If over-issues of bank-notes were responsible in some degree for the speculative mania in England, rather than merely its convenient tools, it was because the divorce of the paper currency from specie made bank-note issues easy and their issuers irresponsible. The proof that the speculative mania was not due entirely to the issues of paper money in Great Britain may be found in the fact that a like condition existed in France, which was upon a specie basis. The liquidation which followed the crisis of 1805 caused coin to pile up in the Bank of France to such an extent that the bank was obliged to invest a part in the obligations of the receivers general and to reduce interest to two and three per cent.[2] Commerce began to expand again in 1808, and the discounts of the Bank of France reached in that year 142,-000,000 francs and in 1810 187,000,000 francs. Numerous failures occurred in 1810, but the leading merchants of Paris

[1] Cunningham, II., 521, note.

[2] Juglar, 406.

kept their heads, discouraged exaggerated speculations, and prevented a serious panic. In England, business came to a standstill, the discounts of the bank dropped from £23,000,000 to £12,000,000 and on April 11, 1811, the Treasury came to the rescue of the market by an advance of £6,000,000 in Exchequer bonds to merchants offering good security. The period of liquidation was made more severe than usual and recovery slower by the great poverty of the crops of 1811. Speculation in agricultural products and land led to the rapid extension of the system of enclosure of land which had formerly been in commons. Such large sums were sunk in fencing and improvements and so much land was brought under cultivation that the fall of prices, upon the close of the Napoleonic wars and the resumption of specie payments, ruined many small cultivators and threw their land again upon the market.[1]

The Crises of 1814–19.

The commercial movements of the second decade of the present century reflected the disturbed condition of public affairs. The policy of crushing each other's trade by paper blockades and interference with the rights of neutrals, which governed England and her allies on one side and France and her dependencies on the other, made commerce like the casting of dice in a game of chance. Markets which had been closed to English and American goods were opened from time to time, with the expulsion of the French from Portugal and Spain and the accession of Russia and Sweden to the coalition against Napoleon. The news of his disasters in Russia in the autumn of 1812 diffused the belief in England that the French Emperor was upon the eve of his downfall and that France would soon be thrown open to the commerce of the world. Speculation ran riot in colonial produce, which it was believed would find a ready market in France at the extravagant prices which ruled there for the small quantities which had escaped the Continental

[1] Cunningham, II., 479.

blockade.[1] The rejection of the recommendations of the Bullion Report and the depreciation of irredeemable bank-notes in England encouraged the delusion that the growth of wealth was commensurate with the rise of prices. Prices reached their maximum at the moment of the abdication of Napoleon in the spring of 1814 and the coming of the general peace. The opening of the Continental markets had been too greatly discounted, goods could not be sold at the prices at which they were held, and the fabric of paper wealth tumbled like a house of cards. The country banks failed by the score in 1815, 1816, and 1817, and the disappearance of their notes so contracted the paper circulation that Bank of England paper seemed for a moment on the point of touching par.[2]

The United States were already feeling the embarrassments of a new country in maintaining an adequate metallic circulation, when the War of 1812 and the financial incompetence of the government precipitated a crisis. The expiration of the charter of the Bank of the United States in 1811 brought many new banks into the field and a veritable banking mania prevailed for several years in the Middle, Southern, and Western States. The offer of the Pennsylvania shareholders of the Bank of the United States to pay a bonus of $500,000 to the State for the privileges of a State charter, and to loan the State $500,000 in addition,[3] aroused such extravagant estimates of the profits of banking that the proposition was rejected and an effort made to secure these profits for local banks. A bill authorizing forty-one new banks was passed over the veto of the governor and thirty-seven of them went into operation in 1814. Similar events occurred in other States, and in two years the number of banks in the United States increased from 88 to 208. The volume of specie was not adequate to support the mass of credit thus attempted to be created and what there was in the country rapidly

[1] Coffee, which was four pence per pound in England, had been selling for four or five shillings in France.—Juglar, 323.

[2] *Vide* p. 111.

[3] McMaster, IV., 287.

drifted to New England, where prices were low and transactions were upon a metallic basis.[1]

It needed but a breath to overthrow credit in the South and West, and the motive came with the capture of Washington on August 24, 1814. The banks of Philadelphia announced their suspension on August 31st, and the banks of New York followed on the next day, and did not resume until after the creation of the second Bank of the United States in 1817. The country was stripped of specie, notes were issued for as small an amount as one cent, and many municipalities put out notes for a few cents, redeemable in bank-notes and receivable for taxes.[2] The period following the war was one of prostration in the United States as well as in Great Britain. The United States were for a short time importers and found the British exporters eager to sell because of the excessive stocks they had accumulated in anticipation of the European peace. But importations fell off as the American people discovered the real poverty with which they had come out of the war. The month of August, 1819, found 20,000 persons seeking employment in Philadelphia, and a similar condition of affairs in the other great cities of the North.[3]

The economic disturbances in England were chiefly monetary in 1817 and 1818, but were intensified by scarcity and the high prices of cereals. The monetary difficulties were due to the steady withdrawal of gold for foreign coinages and in the form of subscriptions to Prussian, Austrian, and French loans. The sum of 125,000,000 francs in gold was coined at the Paris mint, of which three-fourths was estimated to have been drawn from England.[4] France, in the meantime, was paying the penalty of defeat in the field. Commercial affairs were brought nearly to a standstill by the entrance of the Allied armies into Paris in 1814, and they suffered another period of enforced liquidation after

[1] *Vide* p. 315.

[2] McMaster, IV., 297.

[3] Sumner, *History of American Currency*, 79.

[4] Juglar, 327.

Napoleon's return from Elba in March, 1815. France was obliged, after Waterloo, to issue 500,000,000 francs of public obligations to pay the war contributions imposed upon her. The price of securities fell so disastrously that the Minister of Finance came to the rescue of the market and loaned freely to the speculators, in order to maintain prices. The result was to bring the securities raining upon the Paris market and to increase the exportation of bullion.[1] The metallic reserve of the Bank of France fell from 117,000,000 francs on July 1, 1818, to 37,000,000 francs on October 29th. The bank shortened the term of commercial discounts to forty-five days and in 1819 was flooded again with idle capital.

The Crisis of 1825.

The next great crisis which shook the commercial world attained its height in England at the end of the year 1825. The metallic reserve of the Bank of England steadily increased from 1820 until 1823, when it stood at £14,100,000, while the circulation was reduced until it stood at about £16,300,000. The Bank was required by the Act of 1819 to retire its £5 notes by redeeming them in gold within four years. This demand for gold, comparatively trifling in itself, was accompanied by a foreign drain due to the immense loans contracted by the governments of Europe and Latin America and the fever of speculation in domestic and American companies which developed in England. This speculative mania was attributed by Mr. J. H. Palmer, the Governor of the Bank of England, to the reduction of the interest on government securities. He said to the Parliamentary committee of inquiry into the causes of the crisis:

> The first movement in that respect was, I think, upon £135,000,000 of five per cents., which took place in 1823. In the subsequent year, 1824, followed the reduction of £80,000,000 of four per cents. I have always considered that reduction of interests, one-fifth in one case, and one-eighth in the other, to have created the feverish feeling

[1] Raffalovich, *Marché Financier en 1891*, 9.

in the minds of the public at large, which prompted almost everybody to entertain any proposition for investment, however absurd, which was tendered. The excitement of that period was further promoted by the acknowledgment of the South American republics by this country, and the inducements held out for engaging in mining operations, and loans to those governments, in which all classes of the community in England seem to have partaken almost simultaneously. With those speculations arose general speculation in commercial produce, which had an effect of disturbing the relative values between this and other countries, and creating an unfavorable foreign exchange, which continued from October, 1824, to November, 1825, causing a very considerable export of bullion from the bank, about seven millions and a half.[1]

The correctness of these views is supported by the phrensy of speculation which seized the community. The new republics of Latin America, the New European states which had been carved out of the Empire of Napoleon, and the older governments which had incurred heavy war expenses, appeared in the London market as borrowers and the public loans issued within four years were estimated at nearly £50,000,000. Stock companies were formed with objects as indefinite and impracticable as in the time of the South Sea Bubble. One which found subscribers proposed to drain the Red Sea to recover the gold lost by the Egyptians when pursuing the Israelites.[2] It was estimated that £150,000,000 of British money, including that invested in government loans, had been sunk in Mexico and South America alone.[3] Much of it went into mining shares, which advanced fabulously during 1824 and 1825. The Real del Monte shares, on which £70 was paid, were at £550 in December, 1824, and £1350 in the following January. The first payments required did not usually exceed five per cent. of the par value of the shares, so that the humblest were able to count upon enormous dividends from very trifling investments. The number of stock companies created was computed at 624, calling for a nominal capital of £372,173,100. This enormous

[1] Gilbart, I., 65.
[2] Juglar, 334.
[3] MacLeod, *Theory and Practice of Banking*, II., 111

sum, if actually paid in, would have required $1,850,000,000 of capital, and in the England of that day, with her population of 13,000,000, would have represented an investment of nearly $150 per capita, or one-third of the wealth of the country.

The withdrawal of so much capital from legitimate commercial uses as was actually paid into these companies caused a sharp increase in the value of money and the prices of commodities, and manufacturers were forced to borrow money to carry on their ordinary operations at the increased rates. The rising prices in the latter half of the year 1825 reduced purchases, the warehouses began to fill and the owners of merchandise were confronted with the usual dilemma of a commercial crisis,—to sell their goods at a loss or make new loans at higher rates of discount. The coin reserve of the Bank of England steadily declined after March, 1824, when it stood at £13,800,000, until it reached £9,490,420 on January 29, 1825, and £6,659,780 at the end of April. The reserve had been forced down to £3,012,150 on November 26th, and the country banks, which had been increasing their discounts and their note issues, were suddenly brought to a halt by the failure of Sir Peter Pole and Co., on Monday, December 12, 1825. Sixty-three country banks were forced to suspend, and "the consequence," says Mr. Bagehot, "was a panic so tremendous that its results are well remembered after nearly fifty years."

The Bank of England went on expanding its discounts up to the end of April, in spite of an adverse foreign exchange and the rapid reduction of the coin reserve. The process of contraction began in May, but the bank did not raise the discount rate until the panic had actually broken. It was not until December 13th, that they advanced the rate from four per cent. to five. The policy of contraction during the first days of the panic, on Monday and Tuesday, caused absolute paralysis of business. Mr. Huskisson said afterwards in the House of Commons that during these two days, "It was impossible to convert into money, to any extent, the best securities of the government." The usury laws, which

limited the rate of interest outside the Bank of England to five per cent., prevented loans of private capital, which might have been willingly made at seven, eight, or ten per cent. The very desperateness of the situation brought its own remedy in time by forcing the sale of commodities at a ruinous loss, which brought foreign capital pouring back into England in the purchase of goods. The directors of the bank changed their course on Wednesday, enlarged their issues to solvent borrowers, and almost in a moment the panic was stayed in London.

The bank issued upwards of £5,000,000 in notes, between Wednesday and Saturday, by advances on stock and Exchequer bills as well as by discounts,—in the language of Mr. Jeremiah Harman, one of the directors, "by every possible means consistent with the safety of the bank; and we were not, upon some occasions, over-nice." The coin in the vaults of the Bank of England scarcely exceeded £1,000,000 on Saturday night of this eventful week and the influence of the panic had not been fully stayed throughout the country. The clamor for gold was stilled, however, by the free issue of notes and a box of £1 notes was sent down into the country. The Gurneys, who did business at Norwich, displayed piles of notes many feet thick on their counters and prevented a run by the confidence which this exhibition inspired. The aid of the Bank of France was sought and a credit for £2,000,000 opened on three months bills.[1] The sum of £400,000 arrived from France in gold on Monday, the 19th, but the deputy governor of the Bank of England had already given the assurance to Lord Liverpool on Saturday evening that the danger was over in the city and that quiet would soon be restored in the country.

The crisis of 1825 was an essentially English crisis, because loanable capital was more plentiful in England than elsewhere and the speculative mania was mainly confined to the London market. The solidarity of the world's markets was indicated, however, by the appeal to the Bank of France

[1] Levi, 188.

and by the reflex influence of the crisis in France and the United States. The war with Spain caused some curtailment of commercial operations in France in 1823 and broke the force of the ascending movement of business. Much of the gold expelled from England by unfavorable exchanges found its way into the Bank of France, so that when the reflex movement of the English crisis was felt in France in the demand for enlarged discounts, the bank had an ample reserve to meet it. The volume of discounts, which had been 478,000,000 francs in 1824, increased to 638,000,000 in 1825 and 688,000,000 in 1826, and fell to 556,000,000 in 1827 and 402,000,000 in 1828. The ebb and flow of the commercial tide followed, therefore, substantially the same course in France as across the channel, but without such an acute disturbance.[1] The rate of discount was maintained uniformly at four per cent.

The Crisis of 1837–39.

The crisis of 1837 was felt most severely in the United States, but over-speculation in banks and joint stock companies affected Great Britain and the Continent, and Great Britain was affected also by her large loans in America. There were symptoms of a panic in England in 1832, but they arose from political events, aggravated by bad management of the Bank of England, and did not present the phenomena of a genuine economic crisis. The government undertook the conversion of the public debt at three and a half per cent. and the disturbance thus caused in the money market was complicated with the expiration of the charter of the bank and the political convulsions on the Continent. The reform bill was pending in Parliament and the masses were irritated against Wellington and the conservative ministry for their opposition. The circulation of the Bank of England was much less than in 1825 (about £16,800,000), but the coin reserve had been allowed to fall below £5,000,000. The attempt to create a political run upon the bank

[1] Juglar, 410.

caused alarm for a time, but was repressed without serious results.[1]

The crisis of 1837 in the United States was one of the results of that discounting of the future in a new country, which results in over-speculation and the sinking of capital in unproductive enterprises. Foreign capital became available in great quantities for the use of the American people after the recovery from the crisis of 1825 in England, and specie imports kept company with an excess of imports of merchandise, amounting in seven years to $140,700,000, as evidence of the heavy loans which Europe was willing to make in the United States.[2] The fact that the United States succeeded in wiping out their entire public debt and accumulating a surplus seemed, among the financiers of European countries, burdened under millions of debt and annual interest charges, to be a proof of great prosperity.[3] The success of the Erie Canal led to the projection of many similar enterprises in the Middle States and the West; cities were laid out in the wilderness, and city lots sold at prices which in conservative times could hardly have been realized in New York and Philadelphia. The valuation of the city of Mobile in 1831 was $1,294,810; it rose in 1837 to $27,482,961, only to fall in 1846 to $8,638,250.[4] The price of cotton was pushed up, and negroes became as active a subject of speculation in the South as the timber lands of Maine in the North.

[1] Juglar, 342.

[2] The excessive purchases of foreign goods, which did not have to be paid for in either merchandise or bullion, is shown by the fact that the imports from Europe increased from $62,893,883 for the year ending September 30, 1833, to $127,511,020 in 1836, and even the imports from other countries increased from $38,154,060 to $49,068,134. This great increase in consumption was offset only partially by the increase in exports of American merchandise to Europe, which rose from $56,556,837 in 1833 to $96,413,449 in 1836, while other exports slightly fell off. The reaction was striking after the breaking out of the crisis. Imports fell during the year ending September 30, 1838, to $62,017,575, while exports from the United States to Europe fell only to $79,849,768.

[3] Juglar, 464.

[4] Shepard, 251.

Speculation in the public lands ran to extravagant limits. The United States did not advance the price of public lands beyond one dollar and a quarter per acre, which had been fixed by law many years before. The speculators bought of the government at this fixed price and sold on a steadily rising market. The increase in sales of public lands had been comparatively steady and healthful up to 1834, when the sales were 4,659,218 acres and the amount received was $6,099,981. The next year witnessed the sale of 12,364,478 acres and receipts of $15,999,804, and 1836 witnessed sales of 20,074,870 acres and receipts of $25,167,833. The speculative character of these sales is indicated by the steady decline in receipts after 1837, until they fell in 1842 to only $1,417,972.[1] President Jackson began to realize in 1836 the true character of the rush for the public hands and endeavored to check it by the issue of the famous "Specie circular." The circular was the result of the conclusion that the banks organized in the new sections of the West were not safe enough to meet the requirement of existing law, that payments for lands should be received only in specie and notes of specie value. These banks were organized in many cases by land speculators, who issued notes, borrowed the notes and bought the land. The notes received for sales of land were deposited in the bank, increasing its resources, and were then borrowed again for new purchases of land. The "Specie circular," issued July 11, 1836, put an end to this by requiring payments in coin or land scrip, except until December 15th by actual settlers or residents of the States in which the lands were situated.

The shriek of rage which was uttered by the defeated speculators was echoed by the political enemies of Jackson, and the legend still has believers, that the crisis of 1837 was the result of no other causes than the specie circular and the deposit of public funds in State banks instead of the Bank of the United States. The events connected with the discontinuance of deposits in the Bank of the United States and

[1] Poor, 528.

the veto of the charter[1] undoubtedly caused some degree of financial uneasiness at the time, but the causes of the crisis of 1837 lay deeper than merely political events. The inflation of credit which has been attributed by some to the distribution of the public monies among the State banks had already begun before the transfers were made, and the inflation would have been trifling if it had been limited to the amount of the deposits at the time. The deposits were then only $10,000,000, and it is obvious that they would not have been a large factor in a healthy money market and were a still smaller factor in a period of inflated values and extravagant speculation. The deposits increased, however, from $10,000,000 in 1823 to $41,500,000 in 1836.

Congress added fuel to the speculation, and greatly embarrassed the Treasury when the crisis came, by the policy of distributing the surplus revenues among the States. Tariff reductions, although recommended by President Jackson, were not made with sufficient rapidity to prevent the accumulation of a surplus, which amounted, on January 1, 1836 to $26,749,803. This surplus and subsequent accumulations up to January 1, 1837, reserving $5,000,000 for the government, were ordered by the Act of June 23, 1836, to be "deposited" with the several States in proportion to their representation in Congress. Jackson had favored a distribution in 1829,[2] but in 1836 had come to see the dangers of the plan and only reluctantly permitted the bill to become a law. A new element of disturbance was projected into the financial situation by the coinage Act of 1834, which changed the ratio of value of gold and silver from fifteen to one to sixteen to one, in order to promote the circulation of gold.[3] It was the desire of President Jackson and Senator Benton to create a metallic currency, in place of a bank-note currency resting upon insecure foundations, and it was provided, in the bill authorizing the deposit of

[1] *Vide* ch. xiii.

[2] Knox, 169.

[3] The measure was designed to make a market for the gold which was then being mined in considerable quantities in the Southern Appalachian range.

the surplus with the States, that each of the deposit banks should redeem its notes in specie and should issue no notes after July 4, 1836, of a lower denomination than $5. The adoption of a coinage system which sent silver to a premium over gold, at the same moment that it was proposed to exclude small notes from circulation, threatened to leave the country without a medium for small payments, but the breaking out of the crisis and the suspension of specie payments suspended the operation of the new conditions before any considerable amount of gold had found its way into circulation.

Omens of trouble were already in the air in the opening months of 1837. Popular meetings were held in New York for the purpose of protesting against the high prices of provisions and the undue inflation of bank credits. One of these meetings, on February 14th, became riotous, a flour warehouse was gutted, and the military were called out to preserve order.[1] The commercial crash was delayed until April. The news from England indicated a financial stringency there which was soon felt in the United States. One hundred and twenty-eight failures occurred in New York between April 1st and April 11th, cotton fell nearly fifty per cent., the banks of New York suspended specie payments on May 10th, and the banks throughout the country which had not already fallen followed the example of New York within a few days. The deposit banks ceased to pay specie, the public revenues fell off, further deposits of public monies with the States were suspended, and on May 15th President Van Buren called an extra session of Congress for September.[2]

[1] Shepard, 270.

[2] The New York banks resumed specie payments on May 10, 1838, and most of the other banks of the country followed on July 1st. Early resumption was strongly championed by ex-Secretary Albert Gallatin, then President of the National Bank of New York, who was chairman of a committee, appointed by the New York banks as early as August 15, 1837, to confer on the subject with the bankers of other cities. The New York banks would probably have resumed much earlier, but for the dilatory policy of the United States Bank of Pennsylvania.—Stevens, 282–85.

An important incident of the crisis, which affected seriously the Southern States and European investors, was the great speculation of President Biddle of the United States Bank of Pennsylvania in cotton. He undertook to corner the cotton product of the world by arranging with the merchants to make all their consignments to the agents of the bank at Havre and Liverpool. He drew bills on England in 1837 against cotton for £3,000,000, and expected to get the benefit of the difference between the rates at which he loaned in the United States—five and six per cent.—and the English rate of two per cent. But the United States Bank no longer controlled the supply of commercial credit, and the fabulous profits which Biddle appeared to be realizing stimulated the creation of banks all through the cotton belt, which made advances to the planters and undertook to sell cotton on their own account in Europe. The rise of the Bank of England discount rate suddenly curtailed the profits of many of these banks and the Bank of the United States went to their rescue in order to maintain the price of cotton. Bank shares and commercial paper were purchased by Biddle at a discount of more than twenty-five per cent., which were thrown upon the European market and eagerly snatched up at par by European investors, who had not discovered the tottering condition of American finance. But the enterprise was too vast, even for Biddle's resources. The reserves of cotton were brought out, old stocks in the hands of manufacturers were allowed to run down, consumption diminished and mills reduced their output, while bale upon bale continued to pour upon the Liverpool and Havre markets. The House of Hottinguer of Paris protested Biddle's paper, the Hopes of Amsterdam broke off relations with him, and the price of cotton tumbled, in common with that of other commodities.[1]

Speculation in banks and joint stock companies had reached a serious point in England, irrespective of large English investments in America. The growth of the specu-

[1] Juglar, 462–65.

lative spirit did not escape the attention of shrewd judges of the situation, and Lord Wharncliffe as early as August 14, 1834, called attention in Parliament to the extension of joint stock banks and the insufficient capital with which they were trading.[1] The matter was made the subject of a Parliamentary inquiry in May, 1836. Mr. Poulett Thompson, President of the Board of Trade, took part in the debate and said that he had kept a register "of the different joint stock companies, and of the nominal amount of capital proposed to be embarked in them. The nominal capital to be raised by subscription amounts to nearly £200,000,000 and the number of companies to between 300 and 400." "The greater part of these companies," Mr. Thompson observed, "are got up by speculators, for the purpose of selling their shares. They bring up their shares to a premium, and then sell them, leaving the unfortunate purchasers, who are foolish enough to invest their money in them, to shift for themselves." The most extravagant expectations of railway profits and of mining profits absorbed private capital and were preparing the way for a crash, when the failure of the wheat crop in 1836 inaugurated a drain of gold from the Bank of England.

The bullion in the bank in March, 1836, exceeded £8,000,000. From this date it steadily declined, but it was not until July that the bank raised the discount rate to four and a half per cent. and in August to five per cent. The Agricultural and Commercial Bank of Ireland failed in November, and a run began upon the other Irish banks. They had strengthened themselves by drawing gold from the Bank of England to the amount of £2,000,000 and were able to pay specie on demand, but the distrust was so great that Bank of England notes were taken by the Bank of Ireland only in small amounts and at a discount of two shillings and sixpence in the pound. The Northern and Central Bank at Manchester, with a capital of £800,000 and with forty branches, appealed to the Bank of England for help in

[1] MacLeod, *Theory and Practice of Banking*, II., 137.

December, and it was only granted on condition that the institution should discontinue all its branches except at Liverpool, and afterwards that it should discontinue business after February, 1837.[1] The bank was more liberal to some of the large houses with American connections and eventually aided them to the amount of £6,000,000.

The latter half of the year 1837 and the year 1838 showed an increase of the cash reserve of the Bank of England and a reduction in the discounts and circulation. The access of gold to England, however, was due to the abuse of credit in America, France, and Belgium and did not indicate a return of sound conditions at home. Notwithstanding the danger, the Bank of England lowered its discount rate, November 29, 1838, from four to three and a half per cent., and an increase to five per cent. on May 16, 1839, was insufficient to arrest the downward course of the reserve. The suspension of specie payments again stared the bank in the face, offers were made to sell annuities, some public stocks were sold, and drafts were made upon Paris for £600,000 in bills of exchange. The bank was unable to reimburse these drafts when they matured and foreign bankers began to draw upon London for coin. Messrs. Baring and Company came to the rescue and made an agreement with several bankers of Paris to accept bills of exchange to the amount of £2,000,000. A like arrangement with the bankers of Hamburg procured £900,000 more, and on September 2, 1839, when the coin and bullion were at £2,406,000, the decline was arrested.

The Bank of France was fortunately in a position to meet these demands in 1839, for its own coin reserve had increased in January to 214,000,000 francs ($41,400,000). It would have been less easy to spare gold at an earlier date, for the bank had only 105,000,000 francs ($20,000,000) in its reserve in January, 1837, and demands for discounts were rapidly increasing from Paris and the country. The bank was compelled to buy 8,000,000 francs in gold and to import 10,000,-

[1] Gilbart, I., 314.

000 francs in gold bullion.[1] The crisis was less severe in France than in England and the Bank of France was able, at some risk to commerce, to maintain the uniform discount rate of four per cent.[2] The demand for coin and for increased discounts came mostly from the interior of France and while the gold flowed rapidly from the bank into the provinces in 1836, it flowed almost as rapidly back in the second half of 1837. The suspension of the Bank of Belgium in November, 1838, and the disasters in the United States led to an increased demand for accommodation from the Bank of France and discounts rose from 103,000,000 francs in June, 1838, to 228,000,000 francs in January, 1839, but legitimate demands were met without impairing the coin reserve.

The Crisis of 1847.

The crisis of 1847 was so severely felt in Great Britain and France, on account of the failure of their crops, that they were driven to pour their gold and silver into the lap of the United States in the purchase of her bounteous harvests, and the year was for her one of unusual prosperity. The value of the exports of merchandise from the United States for the fiscal year 1847 was $156,741,598, an increase of more than forty per cent. over any preceding year; the excess of exports over imports was $34,317,249, a balance never again attained until 1876; and the imports of gold and silver were $21,574,931,—a total which stood substantially unchallenged until shortly before the resumption of specie payments in 1879. This great prosperity on the western shore of the Atlantic was obtained at the expense of fever, starvation, and death on the eastern shore. A long season of rain and wet rotted the entire potato crop of Ireland in 1845 and 1846 and destroyed the food of a people. The Irish peasant, who had no other means of living, was dying literally by tens of thousands among the marshes and hovels of his native land. Coffins could no longer be pro-

[1] Juglar, 414.
[2] Courtois, 159.

some districts and the coroner refused to go on holdnquests. The population of Ireland was found when amine was over to have shrunken by death and emigran from eight millions to six millions.[1] Three-quarters of on of Irish immigrants reached the United States in decade ending with 1850 and nearly a million followed next.

e great demand for gold to pay for foreign grain was mediate occasion of the crisis of 1847, but there had so a great transformation of circulating into fixed capi in the building of railways, and the effect of the export of gold was much intensified in England by the operation of the Bank Act of 1844. This act did not accomplish its original purpose, to contract domestic circulation in the exact measure of the export of bullion. Had it done so, the effect would have been even more disastrous than was actually the case; but it accomplished, at a time when it was too late to arrest speculation, a needless pressure upon the money market and a sharp contraction of discounts. The railway mania steadily spread in Great Britain for several years. New railway capital was authorized by Parliament in three years to the amount of £221,000,000 and the amount actually expended on railways in two and a half years was computed at £76,390,000.[2] The countries of the Continent had followed Great Britain in railway expansion. Belgium in 1845 had 343 miles of railway, built at a cost of $29,000,000; France 552 miles, at a cost of $51,000,000, with 1900 miles projected at a cost of $150,000,000; Germany, 2000 miles at a cost of $77,000,000, with 2300 miles projected; and the United States, 3688 miles at a cost of $88,000,000, with 5624 miles under construction at an estimated cost of $134,000,000.[3] The effect of this great absorption of the savings of the community in a single class of enterprises was illustrated in an incidental way when Parliament in 1846 required all railway companies intending to apply for

[1] McCarthy, I., 278–82.

[2] Report of the Lords' Committee, Gilbart, I., 337–38.

[3] Levi, 303–304.

incorporation to lodge ten per cent. of their capital within fifteen days after the beginning of the Parliamentary session. It was feared that the notes issued under the Bank Act of 1844 would prove insufficient to make these payments and it was arranged that the £14,000,000 found to be required should be obtained by daily payments deposited in the Bank of England and immediately loaned out again for further payments.[1]

The harvests of 1842, 1843, and 1844 were abundant, large savings were made by the British nation, the quantity of capital required to be invested in goods in stock was reduced by improvements in the means of transit, and bullion rapidly accumulated in the Bank of England. Discount rates at the bank fell as low as one and three-quarters per cent. on the best bills and after some fluctuations stood at three per cent. from August, 1846, to January 16, 1847. The failure of the potato crop in Ireland in 1845, followed by a worse failure in 1846, required the exportation of large quantities of bullion to pay for foreign grain, and the bullion holdings of the bank decreased from £15,163,000 on December 19, 1846, to £9,867,000 on April 10, 1847. The banking reserve in the meantime had fallen from £8,864,000 to £2,558,000. A panic stared the market in the face for a moment and discount among private bankers rose to ten and twelve per cent. The rise in the bank rate, however, stopped the flow of bullion and a sum of £100,000 which had been actually put on shipboard for America was relanded.[2] The pressure passed off for a time and the bullion in the bank at the end of June had increased to £10,526,000 and the banking reserve to £5,625,000.

The relief was only temporary. A series of heavy failures came crowding on each other's heels in August, involving liabilities of £1,200,000 in the week ending August 16th and £15,000,000 by the end of October. Saunderson and Co., a leading firm of bill brokers, stopped payment in the middle

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[1] Gilbart, I., 343.

[2] MacLeod, *Theory of Credit*, II., 796.

of September, heavily involved with leading houses in the corn trade. Firms in the India trade were crippled by the long credits afforded and were compelled to suspend. Merchants whose own business was sound were ruined by their reckless speculations in railroad securities. The directors of the Bank of England realized that heroic measures were required to save the bank and on October 2, 1847, advanced the bank rate to five and a half per cent. and refused to make advances on stock or on Exchequer bills. The bullion had fallen again to £8,565,000 and the banking reserve to £3,409,000. The refusal to make advances on public securities caused wild excitement on the stock exchange, a fall in the price of Consols, and the disappearance of coin and bank-notes into private hoards. The Bank of England was reduced to the choice of bringing business to a standstill, by refusing all further discounts and pulling down the entire commercial structure in a shapeless mass of ruins, or breaking through the shackles placed upon its action by the Bank Act of 1844.

The government waited until the situation was desperate, in the hope that the pressure would pass away, as that of April had done, without the necessity for suspending the law. The reserve dropped to £1,176,000 and the government finally acted, late on Saturday, October 23d, and notified the bank that they would seek a bill of indemnity from Parliament if notes were issued in excess of the limit imposed by the Act at a rate of discount not less than nine per cent. The effect was magical. The knowledge that money might be had to meet demands instantly destroyed the desire for it. The bank prepared £400,000 in additional notes, but it was not found necessary to issue them. Notes which had been hoarded, under the impression that the limit of issues fixed by the Act would soon be reached and all relief cut off from the business community, came pouring from their hiding places; gold which had been stored in safe deposit vaults was brought back to the banks for deposit, and both the bullion and the banking reserve of the Bank of England rapidly returned to safe proportions.

France suffered less keenly than England in 1846 from the insufficiency of the crops, but the exportation of bullion, under the demands of the London market and in payment for grain, carried the reserve of the Bank of France down from 252,000,000 francs on July 1, 1846, to 80,000,000 francs on January 1, 1847. The bank was besieged for discounts, purchased gold and silver in the provinces at a premium, and sold 20,000,000 francs in French securities to the Barings of London for gold. The crisis was so intense that the management of the bank decided on January 14, 1847, for the first time in twenty-seven years, to raise the rate of discount from four to five per cent. The outflow of specie ceased and the reserve rose from 78,000,000,000 francs on January 15th to 110,000,000 francs on March 16th. The Emperor of Russia came to the rescue of the bank and offered to buy French public securities to the amount of 50,000,000 francs.[1] The bank accepted the offer and these securities went to Russia in payment for grain in place of the bullion which would otherwise have been exported. It was well understood in France that the efflux of gold was due to foreign payments and there was no disposition to present bank-notes for redemption in specie for domestic use.[2] The bank was so well equipped with bullion and confidence was so fully restored that France was little affected by the autumn pressure in England and discount was reduced on December 27, 1847, to the standard rate of four per cent. The breaking out of the revolution of 1848 arrested the development of business, and led the bank to seek the suspension of specie payments by authority of the government for the protection of its metallic reserve. The accumulation of bullion was unprecedented from 1848 to 1851 and attained on October 2, 1851, 626,000,000 francs, which was about 20,000,000 francs in excess of the entire circulation of bills.

[1] Noel I., 111. The negotiations were opened by the Russian ambassador at Paris, Count Kisselef, and a deputy governor of the bank went to St. Petersburg to conclude the transaction. The contract was signed March 17, 1847.

[2] Juglar, 417.

CHAPTER XXI.

THE LATER CRISES OF THE CENTURY.

Growth in the Popular Understanding of Crises—The Effect of the Gold Discoveries and Railway Building in 1857 and 1866—The Failure of Overend, Gurney, and Co. in 1866, and of the Barings in 1890—The Economic Effects of the American and Franco-Prussian Wars and the Long Period of Depression from 1873 to 1879.

THE economic crises of the closing half of the nineteenth century have been of wider extent than some of the earlier crises, because of the wider area of modern commerce, and the suffering which they have inflicted has been keen; but they have possessed fewer of the characteristics of unreasoning panic than the earlier crises of the century, because of the more accurate comprehension of the laws of banking which has been diffused in the business community. The panic in England was less intense in 1857 than in 1847, and the serious dangers of the Baring failure in 1890 were warded off by the union of the Bank of England and the great financial houses, without any outbreak of visible alarm. The United States in 1893 passed through an equally trying experience, and runs upon the banks by depositors were several times feared, but no such runs took place except in cases where there were well-founded reasons for distrust.

The Crisis of 1857.

The crisis of 1857 took its direction from two of the cardinal events of the nineteenth century,—the gold discoveries

in California and Australia and the great extension of railways. The gold discoveries worked a revolution in the proportions of the precious metals available for monetary uses, such as had only been worked by the discoveries of the treasures of Mexico and Peru more than three centuries before. The gold product of 358 years, from 1492 to 1850, had averaged only about $9,000,000 per year,[1] when it was suddenly swelled to an average of $133,000,000 from 1851 to 1860. President Buchanan estimated the production of the United States alone for the eight years ending in 1857 at $400,000,000. Prices did not advance in proportion to the increase in the volume of metallic money, because they were regulated by credit and because a large part of the new money was absorbed by the lateral expansion of commerce in quantity, but enterprises of all kinds received a stimulus unheard of in the history of the world.

To this influence of the doubling of the supply of the precious metals, as if by magic, was added the influence of railway extension. The railway mileage built in the United States in 1856 was 3642 miles,[2] and the construction for the nine years ending with 1857 was 21,000 miles. This construction, forming seven-ninths of the entire mileage of the country, had absorbed $700,000,000, largely in foreign capital. England and the Continent had witnessed a similar absorption of circulating capital. Over four thousand miles of railway had been built in England since 1850 at an expense of £150,000,000, doubling the mileage of the country.[3] So rapid was the development in every branch of American life that, in the language of Professor Von Holst, "It was

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[1] Prof. Adolph Soothbeer gives the aggregate production from 1493 to 1850 as 13,258,000,000 marks ($3,150,000,000), and from 1851 to 1885 as 17,810,000,000 ($4,250,000,000).—*Bimetallism in Europe*, Sen. Ex. Doc. 34, 50th Cong., 1st Sess., 78. The production from 1885 to Dec. 31, 1895, was about $1,375,000,000.

[2] Sumner, *History of American Currency*, 180.

[3] These figures are taken from Mr. Rhodes' *History of the United States* (III., 53), who has made a careful compilation of the essential facts of the crisis in this country.

more and more lost sight of, that even in the age of steam, time must remain an essential factor in every process of development." It no longer seemed absurd to project railways into the wilderness, in the confident belief that they would open up new countries and create traffic where none existed. Immigration lent its aid to the natural growth of population, and the American people, under these combined influences, "worked themselves deeper and deeper into the delusion that the fancy could scarcely keep pace with the reality, and were thus led to mould the reality in their minds in accordance with what imagination pictured to them." [1]

There were signs of a tight money market in both the United States and England for several years before 1857. Bad crops and the diminution of foreign investments caused uneasiness among the Western banks as early as the summer of 1853. They drew heavily upon their balances in New York to replace the capital sunk in railway enterprises, and

[1] Von Holst, VI., 104. It was argued at the time of the panic of 1857, and has been maintained since, that the crash was caused by the low tariff of 1846, which led to large exports of specie to make payments for foreign goods and drained the country of metallic money. Mr. Rhodes, who will not be accused of partiality to the administration of either Polk or Buchanan, says that "in this reasoning cause and effect are confused, and in part, at least, inverted. It was the export of specie which increased the importations of merchandise, and not the importations of merchandise which increased the export of specie." He shows that during the nine years ending June 30, 1857, the excess of the exports of specie over imports was $271,000,000, and that during the same period there was a production of gold in the United States of about $477,500,000, leaving a net increase of specie of about $206,000,000. The net increase in specie in circulation shown by the Treasury estimates during this period was only $148,000,000, the remainder having been absorbed in the arts, but this amount was more than sufficient for American monetary uses, and such export of specie as occurred probably tended to restrain speculation rather than stimulate it. Mr. Rhodes expresses his obligations for this part of his history to Prof. Edward G. Bourne of Adelbert College.—*History of the United States*, III., 51–52. Prof. Max Wirth, the eminent German historian of economic crises, makes no mention of the tariff among the causes of the crisis of 1857.

many were compelled to suspend payment. The Crimean War led to speculation in shipping in England and some perturbation in business circles. The anticipation of trouble, however, as the result of the war, made money lenders cautious and prevented serious embarrassment until the summer of 1855. The Bank of England in that year suffered a serious drain of bullion, which carried its supply down from £18,169,000 on June 23d to £11,752,300 on October 13th. This drain continued, in spite of advances in the discount rate by successive steps, from three and a half per cent. during the summer to six per cent. on October 18th, and finally to seven per cent. on November 8th. The volume of trade did not seem to yield to the pressure of high rates of interest, and prices continued to climb upward,[1] but the bullion in the bank was kept nearly stationary through the year 1856. The tightness of the money market continued into the summer of 1857, when on August 17th the bullion stood at £10,606,000 and the rate of discount was five and a half per cent.

The situation in the United States was complicated, as it was in France, by the changes in the metallic circulation caused by the great production of gold. Gold took the place of silver as the overvalued metal at the coinage ratio, was invariably chosen by debtors for payments, and silver, having become the dearer metal, disappeared from circulation, in spite of bimetallic enactments, under the relentless operation of Gresham's law. The Secretary of the Treasury attempted in 1853 to relieve the contraction thus caused by paying for silver at the mint in gold, which would be added to the circulation.[2] The banks, in spite of their rapid increase, were unable to keep pace with the demand for loanable capital which resulted from the fever of speculation.[3]

[1] Juglar, 363.

[2] Kinley, 175.

[3] The number of banks increased from 715 in 1847 to 1416 in 1857, and the loans and discounts from $310,282,945 to $684,456,887. The increase in the note circulation was from $105,519,766 to $214,778,822. The circulation fell in 1858 to $155,208,344 and the specie holdings of

The specie reserves of the New York banks were strengthened for a time by government bond purchases and they were able to expand their loans. Foreign capital continued to flow into the United States and the bubble of speculation to be blown to the extremist tension.

Conditions were ripe both in Europe and America for a crash, when the impulse came on August 24, 1857, from the failure of the Ohio Life Insurance and Trust Co., of Cincinnati and New York, with reported liabilities of $7,000,000. A panic followed on the New York Stock Exchange, stocks fell, money was hoarded and loaned only at extravagant rates, deposits began to disappear from the banks, and late in September a run began on the banks of Philadelphia. They were compelled to suspend specie payments on September 26th and were followed by the New York City banks on October 13th. The early part of October had witnessed the failure of the Illinois Central Railroad, the New York and Erie, and the Michigan Central, and the run upon the New York banks for the withdrawal of their deposits followed close upon these events.[1] Prices of commodities tumbled with the price of stocks and the farmers felt the pinch in the depreciation of wheat, flour and pork as well as in the fall in real estate.

Money continued tight in England up to the autumn of 1857 and many complaints were made against the Bank of England for the high rate of discount. The news of the failure of the Ohio Life and Trust Co. caused intense alarm

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the banks, which had not suffered during the crisis, rose from $58,349,838 in 1857 to $74,412,832 in 1858 and to $104,537,818 in 1859. M. Juglar points out that it was not increase of circulation which caused expansion so much as "the attraction of deposits by high interest and the lending of them to reckless speculators."—*Des Crises Commerciales*, 268.

[1] The New York banks contracted their discounts from $122,000,000 on August 8th to $97,200,000 on October 17th. The constitution of the State of New York forbade suspension of specie payments directly or indirectly, but the judges of the Supreme Court met and agreed not to grant any injunction unless the bank appeared to be insolvent or guilty of fraud.—Sumner, *History of American Currency*, 184.

for the £80,000,000 of English money which was believed to be invested in American securities. A group of speculators added to the alarm in London by forming a combination to "bear" the market, by finding flaws in securities and working through the press to excite general distrust and depress prices.[1] The high rates of interest in New York began to attract gold from Hamburg; the Bank of France lost 25,000,000 francs in a single week, and the bullion in the Bank of England declined to £8,991,000 on October 19th. The great house of Dennistoun stopped payment on November 7th, with liabilities of nearly £2,000,000, the Western Bank of Scotland closed its doors two days later under appalling revelations of mismanagement and loss, the City of Glasgow Bank suspended, and the banking reserve of the Bank of England dropped on November 11th to £1,462,000.

The money actually in London in the banking department of the Bank of England on this eventful Wednesday night consisted of £375,005 in notes, £310,784 in gold coin, and £44,046 in silver coin. The bank could not have held out a day longer under the Act of 1844. It would have been obliged to suspend discounts not later than Friday and this would have been followed by a run for their reserves on the part of the stock banks, the bill brokers, and the private bankers, who had deposits at the Bank of England to the amount of £5,458,000. At the last moment the Bank Act was suspended. A letter reached the bank on November 12th, authorizing them to issue notes in excess of the legal limit, provided they maintained the rate of discount at ten per cent. Public excitement was suddenly calmed, but the demand for discounts continued heavy for more than a fortnight. The bank issued £2,000,000 in notes above the statutory limit, but the maximum in the hands of the public was £928,000 on November 20th. The remainder were added to the banking reserve. The governor of the bank afterwards testified that there was less acute panic in 1857 than in 1847, but that the real commercial pressure was more

[1] *London Times*, Sept. 10, 1857, quoted by Gilbart, II., 337.

intense. This may be judged from the fact that the aggregate loans by discounts and advances on stocks by the Bank of England were £12,645,000 from November 12th to December 1st.[1] Greater caution was shown than on former occasions in reducing the discount rate, and it was maintained as high as five per cent. in 1858 until the bullion had returned to £15,000,000.[2]

France and other countries of the Continent suffered in the crisis of 1857, though less acutely than England and America, because of the smaller scope of their commercial affairs. The establishment of the Second Empire in France gave an assurance of security to the mercantile classes, which was shaken for only a moment at the outbreak of the Crimean War. Business resumed its activity when it appeared that the operations of the war would be confined substantially to the East and the discounts of the Bank of France rose from the maximum of 154,000,000 francs ($29,000,000) in 1851 to 628,000,000 francs ($121,000,000) in 1857. The bank found it necessary to raise the discount rate to six per cent. in the autumn of 1856 and found its specie reserve at Paris reduced in January, 1857, to 72,000,000 francs ($14,000,000). One of the surprising features of the panic of 1857 was the disappearance of gold from circulation in spite of the enormous production of the preceding ten years. The Bank of France was continually in the market as a purchaser of bullion and expended 14,000,000 francs in 1855, 1856, and 1857 in premiums on 1,274,508,519 francs ($250,000,000) in gold bullion.[3]

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[1] Levi, 404.

[2] MacLeod, *Theory and Practice of Banking*, II., 190.

[3] Juglar, 422. This disappearance of gold from sight, when the quantity in the world available for monetary uses had probably increased more than fifty per cent. in ten years, throws an interesting light on the suggestion of Mr. Forssell, the Swedish delegate to the international monetary conference of 1892, that an attempt to create a monetary union wide enough to prevent exports of the metal under-valued in the coinage laws would be followed by its disappearance within the union.—*Conférence Monétaire Internationale*, Procès Verbaux, 246.

Hamburg, with her purely metallic currency, did not escape the violence of the storm. The rate of discount reached nine per cent. and 145 failures occurred, with reported liabilities of $100,000,000.[1] An attempt was made to sustain credit by combination among the leading merchants, but it failed and resort was had to the government, which borrowed 10,000,000 marks from Austria for discounting commercial bills. The Norwegian and Danish governments were also obliged to contract loans for the benefit of the mercantile community, and in Sweden the National Bank was authorized to borrow abroad 12,000,000 rix dollars, to be apportioned among the different towns.[2] In Prussia the Jewish houses suffered more than the banks, and complaint was made that the substantial monopoly of the Bank of Prussia injured credit by the contraction of the volume of circulation. The laws against usury were suspended and the banks were authorized to discount paper secured by either raw materials or manufactured goods.

The Crisis of 1864–66.

The years following the outbreak of the American civil war were years of financial disturbance in both Europe and America, partly as the result of influences set in operation by the war, and partly as the result of independent influences whose effect was intensified by the operation of the others. Periods which witness the turning of business from its ordinary courses into new channels are always periods of uneasiness, of unusual risks and of speculative tendencies. This was the character of the entire period from 1861 to 1866. The great discoveries of gold which had lent their brilliant hue to the dreams of American business men before the crisis of 1857 began to have a more marked effect in Europe a few years later. Their effect was heightened by the fact that at the close of 1861 the banks and Treasury of the United States suspended specie payments and gold flowed

[1] Courtois, 235.
[2] Levi, 405.

with an accelerated current towards Europe. The net gold exports from the United States in 1862 were $21,532,892; in 1863, $56,632,300; in 1864, $89,484,865; and in 1865, $51,882,805. These great additions to the monetary supply of Europe produced only a slight effect upon prices,[1] but they proved a great stimulus to business activity, because of the means of conducting exchanges which they put in circulation in countries formerly without such means. The effect in France is described by an eminent French writer,[2] in the following terms:

> In those *arrondissements* and cantons where formerly the bill was a myth and the gold louis a phenomenon, hundreds of thousands of francs and even millions in specie and in bills are now in continuous rotation, promoting a movement of transactions which grow in intensity and extent day by day. They constitute a potent dike against depression and depreciation. The ancient possessor of monetary capital is neither robbed nor defrauded by this increase in the quantity of instruments of circulation, whether the increase consists in real gold or in credit gold (*or supposé*). On the contrary, he gains as much by it, more perhaps, than the general public. The superior activity of exchanges assures to the aggregate of circulating capital employment more fertile, more constant, and, inasmuch as it stimulates production and renders products more abundant and less dear, it even increases the value and the purchasing power of the pre-existing gold.

The news of war in America had an immediate effect upon the price of cotton and upon the London money market. The first influence upon the Bank of England, before the suspension of specie payments in the United States, was a loss of bullion and an increase of the discount rate on February 14, 1861, to eight per cent. The United States became smaller purchasers than before from Europe and if they had remained on a specie basis might have exacted the price of

[1] Prof. Jevons, who accepts the quantitative theory of money sufficiently to make a careful mathematical calculation of the effects of the new gold, declares "that ten per cent. may be taken as the best approximation which we can get to the rise of prices between 1845–50 and 1860–62."—*Investigations in Currency and Finance*, 58.

[2] Horn, 263.

their exports for a time in specie. The opposite policy caused bullion to flow freely into the Bank of England and permitted the gradual reduction of the discount rate to two and a half per cent. in January, 1862. The high price of cotton still required specie exports, but not to the United States. The blockade of the Southern ports compelled English mills to seek their raw materials in other markets. India, Egypt, and China were appealed to, and it was not possible to compensate this new trade at once by exports of merchandise. It had to be settled, especially in the case of India, by exports of silver from Great Britain.[1] France felt the counterstroke of this movement in the steady export of silver in exchange for gold. Silver was more valuable as bullion than at the ratio fixed by the French coinage laws and was sold at a premium for gold imported from England and the United States. The Bank of France was driven to making its redemptions in gold, in order to prevent a run for silver. The bank not only exchanged 50,000,000 francs in silver for an equal sum in gold, at the coinage ratio, with the Bank of England, but in November, 1860, effected a like exchange of 30,000,000 francs with Russia and in July, 1861, of 6,000,000 francs with the Bank of Italy.[2]

The reduction of the cotton supply, the derangement caused by the new supplies of gold, and the accumulation of capital in Great Britain as the result of the extended use of machinery, gave a feverishness and speculative character to the money market which recalled the manias of 1825 and 1847 in Great Britain and of 1837 and 1857 in the United States. One of the new elements which entered into the problem in Great Britain was the creation of companies of

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[1] The net imports of silver into India for the four years ending March 31, 1866, were 54,094,337 tens of rupees, or 13,523,584 tens of rupees per year, while the bills on India sold by the home government were 29,409,469 tens of rupees, or 7,352,368 tens of rupees per year. The annual average for the five years ending with 1860 was 10,072,495 tens of rupees in silver and 992,569 in bills. The ten of rupees was about equal to £1.

[2] Juglar, 426.

limited liability. Such companies were only created by special charter prior to 1855, and it was not until after the amendment of the Companies' Act in 1862 that their creation attained the proportions of a mania. A new form of financial enterprise which developed was the creation of stock companies to furnish funds for new enterprises upon pledge of their stock. A proposed railway would not await the slow process of placing its stock and bonds among investors, in order to obtain funds to begin construction, but would deposit these securities with a finance company, which would agree to accept its debts for a specified sum. The immediate service rendered by the finance company was simply the use of its name, and the dangers of this method of financing did not become obvious until these long-dated acceptances began to press upon the market. The finance companies were able to sell their own shares at high prices and thus obtained the funds with which to make advances to the railways and construction companies.[1]

This new method of financing, through great capitalists and banking companies, was legitimate within the limits of the strength of the guaranteeing companies, and the prospects of the new enterprises, and it afforded a method of setting in operation at once enterprises for which the capital could not formerly have been found without appealing to the clumsy methods of government finance. The new system was employed, however, without wisdom and sometimes without honesty during the sixties and it soon brought the inevitable crash. One of the most conspicuous of the new finance houses was that of Overend, Gurney, and Co., which made investments in railways in Great Britain, in cotton in the United States, and in new enterprises in India. The company commanded the unlimited confidence of the public, because of the high credit of the private firm which was turned into a limited company in July, 1865. The firm was already in debt at that time to the amount of £2,970,168 and the methods by which this money had been lost were reck-

[1] Levi, 462.

lessly continued by the limited company. The very confidence reposed in the company was to some extent the cause of its later fall, for it invited such large deposits that use had to be found for them at the expense of safety.

The craze for limited companies increased their number in England within a few years by nearly three hundred, with a nominal capital of £504,000,000. Many were abandoned before starting, others went into bankruptcy, and the projectors of some disappeared, leaving no record behind them. The deposits in the London joint stock banks increased from £43, 000,000 in 1860 to £91,000,000 in 1864, and the country and private banks probably held on the latter date £20,000,000 more. A large part of these deposits consisted of acceptances, which were confounded indiscriminately with cash and credits.[1] France had entered upon the policy of "financing," under the encouragement of Napoleon III., even in advance of England, and her great *Société de Crédit Mobilier* for several years paid tempting profits and was the model of similar creations across the channel.[2] But France and the Continent met their crisis in 1864. The rise of prices was arrested in January of that year and the Bank of France, by keeping its discount rate two per cent. below that in London, was obliged to purchase gold, from January to November, to the amount of 221,000,000 francs. Discounts fell off and business for the next six years was kept within conservative limits by the fear of war and the political uncertainties attending the decadence of the Second Empire.[3]

Deficient crops added their influence in 1862 to high prices for cotton to create a balance of trade adverse to England, but it was not until the close of 1863 that the exchanges became adverse, the metallic reserve of the Bank of England fell to £13,000,000, and the discount rate was gradually raised, until in December it stood at eight per cent. Bullion began to flow back into the bank, the rate was reduced,

[1] Juglar, 385.
[2] Levi, 461.
[3] Courtois, 255.

speculation revived, and a new increase to nine per cent. became necessary late in April, 1864. There was another lull until the autumn, when the prospect of peace in the United States caused a tumble in cotton and a smaller fall in prices of all commodities. The bank rate was again advanced to nine per cent. in September, there was an increase of £2,500,000 in discounts, and the pressure for ready money was so intense that Consols fell from 89 to 87. The year 1864 witnessed in a sense two crises in England,—the first resulting in the liquidation of the smaller tradesmen, the second involving the great capitalists. The liquidation of both these classes was completed on the Continent in 1864. The effects of the crisis crossed the oceans to Brazil and Australia and if they were not felt in the United States it was because the events of the war interrupted the regular movements of the economic system. Liquidation was not fully completed in England in the case of the great financiers and the spring of 1866 witnessed an after-clap more severe in its effects than the crisis of 1864.

The first gust of the storm of 1866 was the failure of the Joint-Stock Discount Company in February, which was followed in March by the suspension of Barned's Bank of Liverpool, with liabilities of £3,500,000.[1] The discount rate of the Bank of England, which had fallen to six per cent., was raised to seven per cent. on May 3d, eight per cent. on May 8th, nine per cent. on May 9th, and ten per cent. on May 10th. It was on the evening of the last named day, after banking hours, that the news spread of the greatest failure which had ever taken place in England. An action was pending in the courts against the Mid-Wales Railway Company, to recover £60,000, accepted by them and held by the great house of Overend, Gurney, and Co., and two other firms. Judgment was delivered on May 9th, to the effect that the railway company had no right to accept the bills and that they were of no validity.[2] The decision of

[1] Gilbart, II., 343.
[2] MacLeod, *Theory of Credit*, II., 832.

the court, coming at a season of growing alarm, caused a run upon Overend, Gurney, and Co., by depositors, and on the afternoon of May 10th the firm suspended with liabilities of £18,727,915.[1]

The next day, May 11th, known as "Black Friday," was long memorable in English financial history. Lombard Street became impassable with the surging crowd and extravagant rumors assailed the reputations of the strongest houses. The Bank of England extended accommodations during the day in loans and discounts to an amount exceeding £4,000,000, and the banking reserve was reduced close to £3,000,000. The Chancellor of the Exchequer announced these facts in the evening in the House of Commons and stated that the government had addressed a letter to the bank, authorizing the suspension of the Act of 1844. The announcement was received with cheers and the news had a marked effect in mitigating the panic the next day. The decision to authorize the extra issue was not reached until midnight, and a deputation from the bankers waited upon the Chancellor while the House was in session. One of the representatives of the joint stock banks is reported to have said to the representative of the Bank of England, "I can draw a couple of checks to-morrow morning which will shut you up at once."[2] The letter of the government, signed by

[1] These figures are taken from the report of the liquidators at a meeting for dissolving the company, held in London on November 16, 1893. It appeared that £8,266,048 of the liabilities was on account of bills re-discounted under the guarantee of the company and £6,018,835 was due creditors holding security. The proved claims were finally reduced to £4,913,382, including interest, and they were paid out of the proceeds of amounts realized from bills of exchange and other credits to the amount of £1,982,289; from assets of the old firm, £688,561; separate estates of the partners of the old firm, £909,870; cash and interest on investments, £60,273; and calls of £25 per share upon the shareholders, £2,088,286. The liquidators were enabled to return £626,945 to the contributories, and the various law costs and expenses of the twenty-seven years of liquidation were £188,953.—London *Bankers' Magazine*, Dec., 1893, LVI., 809.

[2] Gilbart, II., 354.

Lord John Russell and Mr. Gladstone, contained the following:

> If, then, the directors of the Bank of England, proceeding upon the prudent rules of action by which their administration is usually governed, shall find that, in order to meet the wants of legitimate commerce, it be requisite to extend their discounts and advances upon approved securities, so as to require issues of notes beyond the limits fixed by law, Her Majesty's Government recommend that this necessity should be met immediately upon its occurrence, and in that event they will not fail to make application to Parliament for its sanction.
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> No such discount or advance, however, should be granted at a rate of interest less than ten per cent., and Her Majesty's Government reserve it to themselves to recommend, if they should see fit, the imposition of a higher rate. After deduction by the bank of whatever it may consider to be a fair charge for its risk, expense and trouble, the profits of these advances will accrue to the public.

The effect of the suspension of the Act of 1844 was so marked that it appeared the next day, which was Saturday, as if the crisis was at an end. The pressure upon the banks ceased for the moment, and the Bank of England did not find it necessary to use the authority to issue notes beyond the legal limits. The demands for discount continued large, but were met from the deposits, which were poured freely into the bank by the outside bankers when they were assured that their appeals for notes would be honored. Large commercial failures began again, however, during the week, which imperilled the banks holding their paper and led to new demands by depositors. The Bank of London paid out fifty per cent. of its deposits in cash and was obliged to stop, with liabilities, according to its last balance sheet, of £4,335,877. The Consolidated Bank came to its rescue, but was in its turn exhausted. The Agra and Masterman's Bank, with wide connections in India and the East, and obligations of £15,582,002, was also compelled to suspend payments. These banks had ample assets, but were unable to convert them into bank-notes and cash rapidly enough to meet the demand of their depositors. The magnitude of the demands upon the Bank of England after the authority was given to suspend the Bank Act, may be judged from the debate

which took place in the House of Commons on the evening of May 17th. The Chancellor of the Exchequer stated, in reply to a number of interrogations:

> The advances made by the Bank of England on government securities on Friday, the day of the panic, amounted to £919,000, on Saturday to £747,000, and on three subsequent days various amounts, making up the total amount advanced on these securities in five days to £2,874,000. Then with regard to the accommodation of commerce in general, the best measure that can be given of the manner in which the bank has exercised its functions is shown in this:—that it has made advances upon bills and has discounted bills to the extent of £9,350,000, making a total of advances and discounts in five days of £12,225,000.[1]

The rate of ten per cent. at the Bank of England was maintained from May 11th, to August 6th, and distrust of English investments was so keen that this high rate failed for a time to attract foreign capital from countries where interest rates ruled much lower. The rate of the Bank of France continued for months at four per cent. and the coin reserves of the bank remained unimpaired.[2] This circumstance was seized upon by critics of the rule of controlling the flow of bullion by the discount rate as proof that the rule was not based upon sound economic law. The simple truth was that the credit of English finance was shaken to its centre. A high rate of interest ceases to attract when grave doubt exists whether the principal will ever be repaid. England paid the penalty for the wide ramification of her credit system, and the severe shock which it received in 1866, in an almost universal fear that her great banks and finance companies, even the Bank of England itself, were on the verge of bankruptcy. The prevalence of a ten per cent. rate for

[1] Gilbart, II., 348.

[2] Liquidation in France had already taken place, in anticipation of war, and the suspension of specie payments in Italy sent large quantities of bullion over the Alps.—MacLeod, *Theory and Practice of Banking*, II., 196-97. M. Horn endeavors to trace the low rates in France to the agitation there against the monopoly of the Bank of France, but if such an influence operated, it was evidently only because other conditions concurred to make low rates safe.—*La Liberté des Banques*, 446.

three months was in itself a heavy fetter upon trade and strengthened the belief that there was something fundamentally wrong with English banking. The distrust abroad was profound enough to justify for a moment the phrase of Sir Stafford Northcote, that there was "a run upon England," and to wound the national pride with the unaccustomed fear that London was about to lose her pre-eminence over the money markets of the world.[1]

In the presence of such fears, an economic law which would operate under normal conditions of credit was temporarily suspended, just as in the past few years foreign capital has been persistently withdrawn from the United States, in spite of tempting opportunities for investment, because of the fear that they would abandon the gold standard. The cherished "convertibility of the bank-note" did not prevent the suspicion abroad that the British government intended to establish forced legal tender, and its intervention to permit the suspension of the Bank Act of 1844 was interpreted among those not familiar with the English banking system as a step in that direction. The Earl of Clarendon gave official testimony to the gravity of the situation, without accomplishing much to relieve it, by issuing a circular letter to the British embassies throughout Europe, stating that "Her Majesty's government have no reason to apprehend that there is any general want of soundness in the ordinary trade of this country which can give reasonable ground for anxiety or alarm, either in this country or abroad."[2] Distrust at home had not at any time extended to the solvency of the Bank of England, after the directors were authorized to borrow from the reserve in the issue department, and the bullion, never below £11,800,000, rose in December to £19,200,000. The discounts, which had risen during the acute stage of the panic to £33,400,000, fell gradually, with liquidations and the slackening of business, to £19,100,000.

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[1] Wolowski, *La Banque d'Angleterre*, etc., 133.

[2] Levi, 471.

The Depression of 1873–79.

The long period of depression which began with panics in Austria and the United States in 1873, and which had hardly terminated six years later, followed some of the most remarkable experiences of the waste of national resources, the sinking of capital, and changes in the economic order which the world has ever seen. National resources were wasted like water in three great wars,—that of Secession in the United States, that of Italy against Austria in 1866, and that of France against Germany in 1870. The direct cost of the American war, exclusive of pensions, was estimated at more than $5,500,000,000, to the government of the United States alone, exclusive of the cost to the South, the injury to private property, and the drain upon the productive power of the country.[1] The cost of the Franco-Prussian War, brief as its military operations proved to be, was estimated at a total, direct and indirect, of $2,700,000,000, of which $2,125,000,000 was the share of France and $575,000,000 the share of Germany.[2] The effect of an important war upon credit is to compel a forced liquidation of business transactions in advance of the time which would be set by the normal movements of a credit cycle. If this was the case during the Napoleonic wars, it has been more strikingly the case under modern conditions, with the great expansion of credit which they have involved. The United States, having escaped the crisis of 1866 by the forced liquidations of 1860 and 1861, was ripe for an explosion in 1873; while France, having been forced to liquidation in 1870, felt only the ripples of the crisis of 1873, which were wafted back from the storm in other countries.

The absorption of capital in great enterprises during the ten years prior to 1873 was as great as its waste in war. The average annual increase of railways in the United States from 1860 to 1867 was 1311 miles. The increase in 1869 was 4953 miles; in 1870, 5690 miles; in 1871, 7670 miles; in

[1] Bolles, III., 244.
[2] Giffen, I., 76.

1872, 6167 miles; and in 1873, after the panic had broken, 3948 miles.[1] The United States did not stand alone in railway expansion. In Russia, a system of 12,000 miles of railway had been almost entirely created since 1868; in Austria, eight years had witnessed an increase from 2200 to 6000 miles; and in South America, nearly $200,000,000 of English capital had been borrowed, mostly for railway enterprises.[2] The result of this network of new lines was the opening of great producing areas, which laid down their harvests in Liverpool and Hamburg at prices which crushed competition, forced down the prices of English and German agricultural lands, and threatened the earnings of the laborer. The great war indemnity paid by France to Germany accumulated such a surplus of loanable capital in the latter country that new manufacturing industries sprung up all over the Empire, which soon outran the demands of domestic consumption, and the agricultural population flocked rapidly from the country to the cities. In Prussia alone 687 new joint stock companies were founded between January 1, 1872, and July 1, 1873, with an aggregate capital of $481,045,000. The construction of the Suez Canal was completed in 1869, destroying the value of much pre-existing shipping, and the development of railway building gave extraordinary activity to mining, forced up the prices of iron and resulted in the establishment of many new foundries in Great Britain and the United States. To these causes of the loss and absorption of capital had to be added, during the period of liquidation, the effect of bad crops in Great Britain and the destruction of vineyards in France by the ravages of the phylloxera, to the value of $2,000,000,000.[3]

The world had gained greatly in productive power during the two decades ending in 1873, but the gain was not sufficient to offset the combined operation of all these causes of waste and these transformations of old conditions. The United States, revelling in the fool's paradise of forced legal tender paper currency, was subjected to several severe heats

[1] Gilbart, II., 388.

[2] Giffen, I., 113–14.

[3] Wells, 23.

and chills, while timid statesmen were waiting for the country "to grow up" to the volume of the currency. Great Britain poured out her capital in foreign loans, as if untaught by the history of previous losses, and the total securities floated were calculated at £505,000,000 in 1872 and £624,000,000 in 1873. The number of joint stock companies formed in Great Britain in 1872 was 1116, with a subscribed capital of £130,000,000, and British exports rose from £199,586,000 in 1870 to £255,165,000 in 1873.[1] Prices were inflated on every European bourse, and when the crash came the fall in securities on the Berlin market alone was estimated at 131,138,000 thalers. Loans taken in London to the amount of £614,228,300 were found wholly or partially in default in 1873 to the amount of £332,399,800 of the principal involved.[2]

Stringency was the chronic condition of the money market in the United States during the closing portions of 1872 and the spring and summer of 1873. The final crash came with the failure of trust companies in New York and Brooklyn early in September, 1873. They were followed on September 18th by the failure of Jay Cooke and Company, who were agents of the government and had been leaders of the powerful syndicate which had handled the refunding of the public debt. Credit was already greatly overstrained, runs took place on the banks of Washington, Philadelphia, and New York, nineteen banks and trust companies closed on September 19th, and the Stock Exchange was closed for ten days. Failures followed each other in quick succession, mills and foundries stopped, production ceased, and for six years the pall of depressed industry lay over the United

[1] The fact that loans are made chiefly in commodities rather than in currency is an important factor in finance and has had much to do with the development of English trade. The exporter furnishes the commodities, which have for him the character of sales for cash, because the bills which he draws are purchased by lenders of capital, for transmission to the borrowing country in payment for the new securities. The borrowing country, being thus permitted to purchase by the evidences of deferred payments, is able to become a much larger purchaser than would otherwise be the case.—London *Bankers' Magazine*, May, 1892, LIII., 739.

[2] Levi, 498.

States. Deposits in the national banks fell from $641,121,775 on June 13, 1873, to $540,510,602 on December 26th. The failures for four years showed aggregate liabilities of $775,865,000 and the railway bonds in default on January 1, 1876, amounted to $789,367,655.[1]

The Secretary of the Treasury endeavored to relieve the money market by paying out $24,000,000 in the purchase of bonds. Little of the money reached the New York banks and they found a more effectual expedient in the issue of clearing-house certificates.[2] This resource had been availed of during the forced liquidations of 1860 and other years of the war, but the amount had never before reached the figures which were attained in 1873. These certificates were issued by a committee, upon the deposit of approved securities by the banks taking out certificates, and were receivable in the settlement of the balances of the several banks at the clearing house. This made them the equivalent of currency in the bank reserves and released a corresponding amount of currency for other uses. The issues of clearing-house certificates at New York on the various occasions of stringency since they were first adopted have been as follows:[3]

YEAR.	FIRST ISSUE.	FINAL CANCELLATION.	TOTAL ISSUE.	MAXIMUM OUTSTANDING.
1860	Nov. 23	Mar. 9, 1861	$ 7,375,000	$ 6,860,000
1861	Sept. 16	Apr. 28, 1862	22,585,000	21,960,000
1863	Sept. 15	Feb. 1, 1864	11,471,000	9,608,000
1864	Feb. 29	June 13, 1864	17,728,000	16,418,000
1873	Sept. 22	Jan. 14, 1874	26,505,000	22,410,000
1884	May 15	June 6, 1884[4]	24,915,000	21,885,000
1890	Nov. 12	Feb. 7, 1891	16,645,000	15,205,000
1893	June 21	Nov. 1, 1893	41,490,000	38,280,000

[1] Wells, 6.

[2] Kinley, 185–86.

[3] *New York Journal of Commerce*, Jan. 16, 1896. The Philadelphia clearing house issued $6,785,000 in 1873. The banks paid six per cent. interest on the certificates held, which ensured their retirement when the emergency was passed.

[4] Except $250,000 issued to the Metropolitan National Bank, some of which were not paid until September 23, 1886.

The crash in Vienna came earlier than that in the United States. The German government became disquieted by the fever of speculation in Prussia and the creation of new joint stock companies, and the paper of many of these companies was refused acceptance by the Bank of Prussia. The speculators transferred their operations to Vienna and in the first quarter of 1873 $140,000,000, of so-called securities, but with little real security behind them, were issued at the Austrian capital. The Bank of Austria was permitted to loan largely on such securities, in order to keep the speculators from failure, but on May 27th, the morrow of the opening of the International Exposition, seventy failures occurred, and on the next day 110, involving establishments of the first importance. The Bourse was closed, the government suspended the limit upon the note issues of the bank, loans were made by the Treasury, and a syndicate of bankers was formed to make advances on sound securities.[1] A general panic was thus prevented, but credit was so far impaired that it was not until 1875 that business in Austria resumed its wonted activity.

The forced liquidations of the Franco-Prussian War caused severe pressure for a short time upon the reserves of the Bank of England; but the early effect of the war, in driving international exchanges to London and Belgium, and sending capital there for safekeeping, was to flood the bank with money and to carry the discount rate downward from six per cent. on August 4th until it touched two and a half per cent. on September 29th. The terms of settlement of the French indemnity kept money in Great Britain for a time, and it was eagerly absorbed at low rates by traders and manufacturers.[2] The determination of Germany to establish the gold standard, and the heavy credits she had accumulated in London, began in 1873 to draw gold away from England, but the raising of the discount rate at the Bank of England, until it touched nine per cent. on September 25, 1873, attracted gold back from the Continent, Australia, and

[1] Juglar, 495.
[2] Gilbart, II., 385.

India, and 1873 and 1874 passed away with comparatively little disturbance.

The crisis in Great Britain was delayed until 1875, when several large firms doing business in South America went down. In May came the collapse of the Aberdare Iron Company, with liabilities of over £1,000,000, which dragged down two other large concerns and the brokerage firm of Sanderson and Company, with liabilities of about £7,000,000. The banks maintained a firm front and actual panic did not occur until June 15th, when Alexander Collie and Company, East India merchants, failed, with liabilities estimated at £3,000,000. Thirty firms followed them into the ditch during the following week and it was found that these firms, as in the case of those connected with the Aberdare Iron Company, were simply tools of Collie and Company, in floating their paper. The Bank of England was well equipped with bullion and notes, and sound firms were liberally assisted, without any advance in the rate of discount, which was only three and a half per cent. Many small firms went to the wall, but Great Britain was touched lightly by the crisis and confidence was only briefly shaken in 1875. The experience of 1878, when the City of Glasgow Bank failed with liabilities of £12,404,297, was also creditable to the soundness and conservatism of British banking. The banks increased their deposits in the Bank of England £7,000,000, while they drew down the cash reserves of the bank about £4,000,000. They thus strengthened themselves by actual cash in hand or credits on the Bank of England to the amount of £11,000,000. Several important failures occurred during the autumn of 1878, including that of the West of England Bank at Bristol, on December 9th, with liabilities of about £5,000,000, but the crisis gradually passed off during 1879 without a general run upon the solvent banks.

The Crisis of 1882–84.

The crisis in 1882 in Europe, which reacted upon the United States in 1884, was most severe in its economic ef-

fects in France, which had escaped the effects of the crisis of 1873 by the forced liquidation of the Franco-Prussian War. The severity of the crisis in France was due in a large measure to the education in the employment of negotiable securities which was afforded by the payment of the great war indemnity. The masses of the French people, little accustomed up to that time to any form of saving but in coin and lands, emptied their hoards in the purchase of national securities, partly from a great outburst of patriotic feeling, but partly also because they felt that the guarantee of the government gave safety and tangibility to engraved pieces of paper, which under other circumstances they would have refused to look upon as a sensible investment. The habit of accepting such securities once formed, and the advantage derived from their regular returns once enjoyed, it became easier to tempt the French peasant and workman to experiment with other securities of a less certain guarantee.[1] Investment societies, trust companies, and syndicates sprang up like mushrooms in the speculative atmosphere of Paris, and those which were upon too grand a scale for any but the great financiers and the rich had their imitators among the adventurers of the street, who accepted gratefully in instalments the petty savings of the poor.[2] The loans of the *Crédit Foncier* swelled from 50,000,000 francs in 1879 to 278,000,000 francs in 1881, while the *Crédit Général Français*, the *Union Générale*, and the *Banque de la Loire* were types of great investment companies whose shares ran brief careers of extravagant advances in price.[3]

It was not in France alone that speculation assumed a new development in the eighth decade of the century. Speculation in earlier times had been largely limited to the raw materials and finished products of commerce, and the bursting of the bubble had come when high prices made goods unmarketable and continuances of loans at the old rates could no longer be obtained at the banks. The much more

[1] Leroy-Beaulieu, II., 218.
[2] Jannet, 385–86.
[3] Juglar, 435.

complicated structure of modern commerce, the distribution of risks by margins and futures, sales for *report* and arbitrage, and the diffusion of savings and the taste for investment among all classes in civilized states, have given a new character to speculation and made the stock market a more sensitive barometer of business conditions than the more sluggish merchandise markets. Securities have become the most convenient means of settling international balances, and by their unrecorded transfers have impaired the value of the statistics of visible commerce. They have become in a large measure a substitute for money and have to be considered in dealing with monetary problems. The steady rise of national securities in recent years has been chiefly the result of the falling interest rates on capital and their safety as temporary investments, but shrewd speculators, by playing upon the ignorance of investors, have convinced them that the other securities upon the market were sure, in their hands, to pursue the same ascending course. Intoxicated by this prospect of paper riches, investors have measured their expenditures by their assumed wealth, have furnished occupations for the ministers of luxury, and have brought perturbation into the entire economic order.[1]

Marginal profits in stock speculations depend in several ways upon low rates for money, and these disappeared in England and France during the autumn of 1881. The United States resumed specie payments on January 1, 1879, and the current of gold drawn towards the country by the operations of the treasury was swelled by the abundant crops and large exports of the years which immediately followed. The merchandise exports from the United States in 1881 were

[1] "These effects of growing wealth have their effect even upon the public finances. Transactions being more numerous and being made at higher prices, the registration taxes give larger revenues. It is thus, that from 1875 to 1881, the receipts of the Treasury exceeded the official estimates by 580,701,788 francs, and this was made the occasion by the party in power for launching into foolish expenses, in the famous plan of public works of M. Freycinet and the purchase of little railway lines, which resulted in a series of loans in profound peace."—Jannet, 392.

$902,377,346,—an amount never before equalled, and never equalled afterwards until 1892. The excess of exports over imports of merchandise was $264,661,666 in 1879, $167,683,912 in 1880, and $259,712,718 in 1881. Europe was suffering from a deficiency of crops, for which, in the language of Mr. Wells, "in respect to duration and extent, there had been no parallel in four centuries."[1] The tide of gold, which had been outward for sixteen years, turned towards America in 1878, and the net gold imports were $77,119,371 in 1880, and $97,466,127 in 1881. The Bank of France found its reserve falling in the autumn of 1881, and endeavored to avoid too sharp an advance in the discount rate by paying light coin and charging a premium for bullion. The Bank of England raised its discount rate on October 6th from four to five per cent., and the Bank of France followed with a like advance on October 20th. The crash came in Paris and Lyons in January, 1882, with the collapse of the *Union Générale* and a fall in all classes of securities. The Lyons brokers sought and obtained succor from the Bank of France, to the amount of 100,000,000 francs, upon securities which would not ordinarily have been accepted, and the Paris agents of exchange obtained 80,000,000 francs, upon the guarantee of a syndicate of bankers. The sum of £924,000 was withdrawn from the Bank of England for France on January 30th, and £2,000,000 was drawn out during the week. The Bank of England discount rate was advanced on February 2d to six per cent., and private bankers, contrary to their usual custom, raised their rates to that of the bank.[2]

The counter-stroke of the crisis in the United States, which was delayed until 1884, was more financial than economic, but the multitude of failures caused intense alarm for a time and threatened to bring business to a standstill. The Marine Bank of New York suspended on May 5th, closely followed by the failure of the Metropolitan Bank, the exposure of the peculiar methods of John C. Eno, Ferdinand

[1] *Recent Economic Changes*, 6.

[2] Juglar, 396.

Ward, and George I. Seney and the collapse of smaller houses connected with them. Money went to one per cent. a day, the interior banks began to draw heavily upon their New York reserves, and it was hardly possible to obtain cash or credit upon the best securities.[1] The decision of the associated banks to issue Clearing-House certificates calmed the storm by degrees, but the failures of the year were computed to show liabilities of $240,000,000,[2] and deposits in the national banks fell from $1,060,778,388 on April 24th to $979,020,349 on June 20, 1884.

The Crisis of 1890.

The crisis of 1890 afforded a striking illustration of the better understanding of such events which has arisen within the past half century, and of the success of skilful and courageous financiers in dealing with them. The particular cause of the crisis was the heavy loans through the Barings to the Argentine Republic, but the years preceding 1890 had been marked, as in other such periods, by excessive speculation, the increase of joint stock companies and the inflation of prices. A part of this tendency to speculation was attributed, as in the case of the crisis of 1837, to the conversion of the public stocks or Consols in 1888, under the management of Chancellor Goschen, from three per cent. to two and three-quarters per cent. The returns of the registrar of joint stock companies showed the total amount of capital registered during 1888 to have been £353,781,594, and in 1889 £241,277,468, while the loans to the Argentine Republic alone in those two years were stated at £36,102,766 in 1888, and £29,223,341 in 1889.[3] Railway earnings

[1] It is apropos of this crisis that Mr. Henry Clews remarks that, "Were the banks allowed to use their reserves under such circumstances, a fund would be provided for mitigating the force of the crisis, and the danger might be gradually tided over; but, as it is, the banks can legally do little or nothing to avert panic; on the contrary, the law compels them to take a course which precipitates it."—*Twenty-eight Years in Wall Street*, 161.

[2] Juglar, 477.

[3] *Journal of the Institute of Bankers*, Jan., 1891, XII., 1.

were increasing, clearing-house transactions were multiplying, and the securities of the South American republics were eagerly accepted by investors under the endorsement of such a house as the Barings.

Money had been poured into the Argentine Republic for the development of banking, public works, and retail trade, until the natives might well have been convinced that their credit in London was without limit. A boom began in 1886 which carried up the price of lands, which a few years before could be had almost for the taking, to $50,000 per league, while suburban lots bounded upward from a few cents to several dollars per square metre. Extravagance and luxury ruled among the governing classes, and the banks which were opened in 1887 under the Guaranteed Banking Law advanced money without security, by the hundreds of thousands to men of prominence and by the thousands to their humbler followers. The requirement of payment by instalments disclosed the fact that the banks had made many bad debts, and it soon appeared that these had been covered up for a time by fraudulent over-issues of bank-notes. The legal circulation, which amounted to $160,000,000, or about $40 per capita, was increased by the fraudulent issue of $50,000,000 to $60,000,000 in additional paper. The National Bank, alone, exceeded its limit $26,000,000. Notes supposed to be redeemed were constantly reissued, and when the crash came paper money was so discredited that gold went to a premium of three hundred in paper, and tickets for a few cents were issued by barbers and retail stores to take the place of the small coins which disappeared.[1]

The interest rate at the Bank of England was gradually lowered during 1890, from six per cent. on February 20th, to three per cent. on April 17th, where it remained until June 26th. It was then raised to four per cent., and afterwards to five per cent., where it stood on Thursday, November 6th. Uneasiness began to be felt among well informed bankers over the increase in the acceptances assumed by the Barings

[1] "Gaucho Banking," London *Bankers' Magazine*, Jan., 1891, LI., 37-47.

and other houses, and the decline of securities indicated a more pressing demand for money and a slackening of business activity. The bank rate was advanced to six per cent. on Friday, November 7th, and ugly rumors were afloat in Lombard Street. The real cause of the uneasiness among the great financiers did not, however, become public property until a week later. It was made known on November 8th, to the Governor of the Bank of England, Mr. William Lidderdale, fortunately a man of great ability and decision of character, that the Barings were on the eve of suspending payment, with liabilities of £21,000,000.

Mr. Lidderdale believed, in spite of the unfortunate history of previous crises, that measures could be adopted which would prevent a crash. He accordingly perfected arrangements within the following week, by which the Bank of England was able to announce on November 14th that all the liabilities of Baring Brothers and Company would be provided for by the bank, and that any loss to the bank would be made good by a circle of guarantors embracing the greatest institutions of Great Britain. The joint stock banks of London, the leading banks of the provinces, and the joint stock banks of Scotland entered into a combination aggregating £15,000,000, "to make good to the Bank of England any loss which may appear whenever the Bank of England shall determine that the final liquidation of the liabilities of Messrs. Baring Brothers and Company has been completed, so far as in the opinion of the governors is practicable." This guarantee was to continue for three years, and afforded absolute assurance to the business community that no great losses to individuals and respectable houses would occur. The Chancellor of the Exchequer was in constant consultation with Mr. Lidderdale while the negotiations for the guarantee were going on and offered him the benefit of the suspension of the Bank Act of 1844, so as to permit the issue of additional notes, if he thought it desirable, but Mr. Lidderdale declined to foster alarm by admitting the necessity for the classic remedy of the great crises of 1847, 1857, and 1866.

Mr. Lidderdale preferred to keep within the law, and at the same time to equip the bank with the means of meeting heavy demands for notes, by borrowing gold from France, Russia, and other sources. The sum of £3,000,000 in gold was brought over under a special contract with the Bank of France,[1] £1,500,000 was obtained from St. Petersburgh, and £500,000 was drawn from other sources. All this sum of £5,000,000 thus became available as the guarantee of additional note issues if the pressure for money should become serious. Mr. Lidderdale would not even alarm the community by forcing up the rate of interest to an extreme point, but maintained it at six per cent. and insisted that the great joint stock banks should continue discounting, as usual.[2] These measures were so successful that the period of stress was passed without actual panic and liquidation set in without important failures. The note issues of the Bank of England increased from £34,507,580 on November 12th to £39,939,900 on November 26th, but the increase was almost exclusively in the notes held in the banking department and there was no unusual pressure for currency.

The firm of Baring Brothers and Company was reorganized as a limited company with a capital of £1,000,000, and made arrangements to continue business. The affairs of the Argentine Republic were found in an extremely bad shape and have not yet been entirely adjusted, but the surplus resources of the Barings enabled a gradual reduction of their liabilities outstanding at the time of the failure. The adjustment proceeded so rapidly that Mr. David Powell, the Governor of the Bank of England, was able, at a general court held on March 16, 1893, to make the following report :[3]

The liabilities, which have been increased during the past six months by a claim from the executors of the late T. C. Baring, now

[1] This loan was secured by the deposit of Exchequer bonds issued to the Bank of England by the British Government, in exchange for national debt stock. The cost of the transaction was £100,000, besides interest.—*Pol. Science Quar'ly*, March, 1894, IX., 23.

[2] MacLeod, *Theory of Credit*, II., 836.

[3] London *Bankers' Magazine*, April, 1893, LV., 610.

stand at £4,558,813, while the value of the assets under the new estimate stands at £4,908,935, giving an apparent surplus of £350,122. It will be seen that progress, though not so rapid as in the previous six months, has been made in the liquidation, the debt to the bank having been reduced in the past six months by £625,000. It may be well, however, to remind you how much has been effected since the guarantee was set on foot. The liabilities, which in the aggregate reached a total of £30,313,000, have been reduced, in a period of about two years and a quarter, to £4,558,813; nearly the whole of the "bills receivable," "remittances to come forward," etc., amounting to £21,193,664, have been got in without loss, and securities have been realized to the value of £4,560,523. It will be remembered that the period of three years, for which the guarantees were originally given, will expire in November next, and, looking to the question how far the liquidation could be carried out without material loss before that date, it was felt desirable, in the interests of the guarantors, that the time should be extended; and I am happy to be able to say, that practically the whole body of guarantors have consented to continue their guarantee for one-fourth of the original amount—which is all that is required—for one year certain from November next, and for a further period of one year if deemed expedient in the interests of the guarantors.[1]

The intimate connection between the world's markets is indicated by the fact that the withdrawal of British deposits in Australia caused a stringency which foreshadowed the crisis of 1893, and that the Imperial Bank of Germany forbore for a time making drafts upon London.[2] The stringency which occurred in the United States, however, in the autumn of 1890 came before the Baring crisis and was less intimately related to that event than to the accumulation of surplus revenues in the Treasury. This had been so serious a danger for several years that Secretary Fairchild in 1888 deposited a large part of the surplus in national banks, while he extended the policy, which he had already inaugurated, of purchasing unmatured bonds at a premium. The purchase of bonds was continued by Secretary Windom, and was pursued on a large scale during the summer and autumn

[1] The guarantors were relieved of further liability towards the close of 1894, and the further settlements were undertaken by a private company.

[2] Jannet, 113.

of 1890. "The amount of public money set free within seventy-five days by these several disbursements," Secretary Windom declared, referring to circulars issued up to September 6th, "was nearly $76,660,000, and the net gain to circulation was not less than forty-five millions of dollars, yet the financial conditions made further prompt disbursements imperatively necessary."[1] Another offer to purchase these bonds was issued on September 13, 1890, and the total disbursements between June 30th and the close of September were $98,276,682, of which $75,828,200 was on the principal of bonds redeemed and the remainder for interest and premiums. The resources of the Treasury were practically exhausted and no assistance could be given to the money market when the reflex action of the Baring crisis was felt two months later in the United States. A number of important failures occurred, but the more disastrous results of the exhaustion of the Treasury were reserved for 1893.

[1] Finance Report, 1890, xxix.

CHAPTER XXII.

THE CRISIS OF 1893.

The Reverberation of the Baring Crash over Europe, America, and Australia—Distrust of American Silver Legislation—The Failure of the Brussels Conference, the Suspension of Free Coinage in India, and the Coming of the Panic—The Shrinkage of Values—Repeal of the Sherman Law and the Bond Contract of 1895—Land Speculation and Bad Banking in Australia.

THE financial crisis of 1893 was in a large measure an afterclap of the Baring failure in 1890. Many millions of British money had been invested in American and Australian securities and the discredit which fell upon Argentine and other South American investments with the failure of the Barings resulted in an irresistible movement to unload such securities and transfer European capital to home investments. Such a tendency would in itself have seriously crippled the great enterprises carried on in the United States, South America, and Australia on foreign capital, even if those countries had not been in any way at fault. Results proved that, while credit rested upon no such rotten basis in the United States and Australia as in Argentina, there had been much sinking of circulating capital in unproductive enterprises and a tendency towards unwise economic policies which had fettered the industries of those countries and driven gold from its legitimate place in their monetary circulation. Circumstances which might have impaired American and Australian credit under any conditions were emphasized by the general distrust aroused by the Baring failure and it required only the rude test of the withdrawal of foreign support to confirm the suspicions of foreign inves-

tors and bring to a head the real evils of the economic situation.

The first shock was felt in Australia, whose people had been congratulating themselves upon their rapidly accumulating wealth and their swelling bank credits, based in reality upon inflated valuations of real estate and of agricultural products. The shock was soon communicated to the United States and its reverberations affected the stock markets of Berlin and Vienna, checked the efforts of Austria-Hungary to establish the gold standard, and drove Austrian securities homeward from Germany as the result of the scramble for ready cash in the Berlin market. Italy was affected by the prevailing distrust, and the evils generated by corruption among her bankers and public men were intensified by the return of Italian securities and the steady outflow of gold and even of subsidiary silver coins under the pressure of a depreciated paper currency. The *Crédit Mobilier Italien*, with a capital of 75,000,000 lires ($14,500,000), was forced to suspend by the difficulty of calling up advances, with deposits of 50,425,000 lires and advances of 89,109,000 lires.[1] France saw her importations shrink from 4,767,867,000 francs ($920,000,000) in 1891 to 3,936,720,000 francs ($760,000,000) in 1893. Even Turkey suffered from the fall in the prices of the products of agriculture, which constitute the larger part of her exportations. Opium within the space of a few years fell twenty-four per cent., wool fifteen per cent., and raisins eight per cent.[2]

The crisis in the United States attracted the most attention, because of the magnitude of their commercial interests and of the investments of foreign capital in their railways, breweries, cattle ranges and public securities. Foreign investments in the United States would have required large payments to Europe prior to 1893 if American enterprises had not proved up to that time so attractive that the interest upon them was constantly reinvested. The result, according to the acute observation of M. Arthur Raffalovich, was

[1] *Revue des Banques*, Jan., 1894, XIII., 15.

[2] *Revue des Banques*, Aug., 1894, XIII., 166.

that "the true indebtedness of the United States abroad had been completely hidden by the influx of foreign capital. What the nation had to pay in interest on railway and municipal obligations and industrial investments had never been felt as a charge upon commerce, in consequence of the compensation which resulted from the uninterrupted entry of capital placed by Europe."[1] The withdrawal of this capital,—even the mere suspension of the process of reinvesting it,—meant heavy payments in gold or merchandise to Europe, without compensation in returning gold or goods. The annual payments required to Europe, outside those compensated by American exports, were estimated by Mr. Heidlebach, a New York banker, at $350,000,000, and the principal of the debt upon which interest was due was computed at not less than two billions of dollars.[2] The withdrawal of a large portion of this productive loan was the price which the United States were called upon to pay for political manoeuvres which aroused the fear that they would abandon the gold standard and make silver the basis of their monetary system.[3]

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[1] *Le Marché Financier en 1893–1894*, 255.

[2] These figures were largely mere estimates until a careful computation was made in the *Journal of Commerce and Commercial Bulletin*, July 8, 1895, based upon inquiries among brokers, steamship agents, and others possessing actual knowledge. This investigation made the total annual indebtedness to Europe, exclusive of merchandise movements in either direction, $175,475,000 and the credits on the other side $29,750,000, leaving a net indebtedness by the United States of $145,725,000. The leading debtor item was $90,000,000 on investment account, which would represent a capital of at least $2,500,000,000. The creditor items included $14,000,000 brought by immigrants, $14,850,000 for outlays of foreign vessels in American ports, and $1,900,000 for outward earnings of American vessels. These figures take no account of the portion of the annual debt which may be settled by new securities.

[3] This tendency to the withdrawal of foreign capital was observed to some extent after the passage of the Bland bill and the Senate resolution offered by Senator Matthews of Ohio, that the obligations of the United States were legally payable in silver. *Vide London Economist*, September 28, 1878; Leroy-Beaulieu, II., 229. The tendency only became marked, however, after the passage of the law of 1890.

A combination of influences worked together to induce an unhealthy condition of industry and finance and to bring about the collapse of 1893. The passage of the Sherman silver law of 1890 was not the absolutely unique cause of the crash of three years later, but it contributed powerfully to that result, indirectly as well as directly. The withdrawal of gold from the United States Treasury pursued an almost uninterrupted course from the moment of the enactment of the Sherman silver law until the outbreak of the panic. The following table, brought down for convenience to a more recent date, will show the progress of this depletion of the gold reserve:

DATE.	TOTAL GOLD IN TREASURY.	GOLD CERTIFICATES IN CIRCULATION.	NET GOLD RESERVE.
February 28, 1889	$326,456,697	$130,210,717	$196,245,980
June 30, 1889	303,504,319	116,792,759	186,711,560
December 31, 1889	313,818,941	122,985,889	190,833,052
June 30, 1890	321,612,424	131,380,019	190,232,405
December 31, 1890	293,020,214	144,047,279	148,972,935
June 30, 1891	238,518,122	120,850,399	117,667,723
December 31, 1891	278,846,750	148,106,119	130,740,631
June 30, 1892	255,577,705	141,235,339	114,342,367
December 31, 1892	238,359,801	117,093,139	121,266,663
June 30, 1893	188,455,432	92,970,019	95,485,413
December 31, 1893	158,303,779	77,412,179	80,891,600
June 30, 1894	131,217,434	66,344,409	64,873,025
December 31, 1894	139,606,354	53,361,909	86,244,445
June 30, 1895	155,893,931	48,381,569	107,512,362
December 31, 1895	113,198,707	49,936,439	49,845,507
March 16, 1896	171,356,965	43,426,829	127,930,136

Gold exports began in large volume the month the Sherman law was approved and reached a total in the fiscal year 1891 of $86,362,654; in 1892 of $50,195,327; and in 1893 of $108,680,844. There were imports during the months in which the American crops were marketed, but the three years contributed an excess of exports of $68,130,087 in 1891, $495,873 in 1892, and $87,506,463 in 1893. The theory of Gresham's law, that the departure of gold denotes the presence of a poorer currency behind the gold, expelling it from the country, was verified by the manner in which the

gold went out as the new Treasury notes were pumped into the circulation at the rate of $4,500,000 per month. The Treasury notes issued undes the Sherman law up to June 30, 1893, were $147,190,227; the net gold exports from the United States from June 30, 1890, to June 30, 1893, were $156,132,423; and the reduction of the aggregate gold in the Treasury during the same period was $133,156,991. Other causes than the mere addition of the notes to the circulating medium doubtless contributed to the expulsion of gold, but the coincidence of these three items,—the loss of gold by the Treasury, its export from the United States, and the issues of notes,—is at least striking.

From the moment that the Sherman law was enacted, the Treasury of the United States was under the necessity of constant expedients to keep its gold and replenish it when it was lost. The government availed itself of every opportunity to obtain gold in exchanges when there was a demand for small notes by offering greater conveniences to those who tendered gold in exchange for paper than to those who tendered other forms of currency. Appeals to the generosity and patriotism of the national banks, which still held a considerable reserve of gold, were frequently made during the autumn of 1892 and the early months of 1893. New appeals of this sort were made under the administration of President Cleveland and the gold reserve was increased from $90,722,958 on June 10, 1893, to $97,286,677 on July 10th, by the efforts of a banking combination in New York, and by leading bankers of Boston, Baltimore, Chicago, and Philadelphia.

These devices were unavailing to permanently arrest the combined effects of the infusion of paper into the currency and the period of speculation and large imports of foreign merchandise which had set in. Funds were raised for working alleged tin-mines in South Dakota; vast tracts of land were purchased in Florida to be unloaded as sugar lands upon foreign investors under the guarantee of the government bounty upon sugar; and new towns sprang up all over the South, dowered in the imagination of their projectors

with infinite possibilities of mineral wealth and manufacturing development, but which proved in fact little more than bottomless pits for the millions of northern capital spent in laying them out. It was the same with suburban improvements in the neighborhood of the great cities as with the "boom" towns of the South. Millions were sunk in improvements, in advance of actual demand, upon property for which no purchasers could be found when people began to ask themselves what was the basis of reality beneath inflated and fictitious values. Railroad building was not so marked a feature of the years preceding the panic of 1893 as of earlier panics, but there was a great demand for capital for equipping street railways with new power and the railways, as usual, were among the first to feel the effects of slakening industry.[1] The conviction that the country was upon the high road of prosperity led to extravagant expenditure by individuals, corporations, municipalities, and the Federal government. Foreign goods poured into the country at an accelerating velocity until the volume of imports rose from $745,131,652 in 1889 to $866,400,922 in 1893. The scarcity of the crops in Europe in 1891 caused a great demand upon the United States to supply the deficiency, and American exports of $1,015,732,011 in the fiscal year ending June 30, 1892, offset in a measure the stream of imports, arrested the loss of gold, and delayed the crisis which might otherwise have sooner followed the operation of the Sherman law.

The relief which the farmers were thus enabled to bring to the fiscal situation of the country was but temporary. Europe was just recovering from a crisis and a part of the

[1] A list of dividends paid in 1893 which had ceased to be paid in 1895 showed a total of $61,710,000 per year. Capitalizing this at five per cent. and making an addition for smaller concerns not included in the list, "the bad investments of the public, within three years, came fully up to $1,500,000,000 and are likely to exceed it."—"Matthew Marshall" in *New York Sun*, July 1, 1895. This list included no losses on real estate investments and none in industrial enterprises, except a few of the largest, whose shares were the subject of trading on the New York Stock Exchange.

payment for the crops of 1891 was made by the return of American securities instead of the shipment of gold. American exports of merchandise fell in the fiscal year 1893 to $831,030,785 and the balance of trade against the United States for the six months ending June 30, 1893, was $68,800,021. The national banks of the East, warned by the European crisis, began to scan their loans and strengthen their gold holdings.[1] The failures reported by Bradstreet's Commercial Agency in April, 1893, were 905, as compared with 703 in the same month of 1892, and the number increased to 969 in May as compared with 680 in May of the year before. The panic did not become acute, however, until the middle of May. The Chemical National Bank of Chicago, with a capital of $1,000,000, closed its doors on May 9th, and was followed two days later by the Columbia National Bank of Chicago, with a capital of an equal sum. These suspensions, accompanied by the collapse of private and State banks and business firms and corporations, paralyzed credit and brought the country to the verge of a crisis.

Upon these conditions of unstable equilibrium came the shock of the suspension of silver coinage in British India. There, as in other silver using countries, the fall in the gold price of silver had brought changes in values and difficulties of administration and exchange. The United States had been making efforts for seventeen years to avert the effects of the depreciation of silver by means of an international bimetallic union. Congress by a joint resolution of August 15, 1876, appointed a joint committee of eight members, known as the "Silver Commission," which submitted an elaborate report on March 2, 1877. The majority of this commission reported in favor of "the restoration of the

[1] Their gold holdings increased $22,000,000 during the year ending September 30, 1892, which, says Comptroller Hepburn, "coupled with the known fact that many State banks and trust companies have also fortified themselves with a gold reserve during the year, shows that the fear that we were drifting towards a silver basis was not confined to foreigners." This is dated December 5, 1892, six months before the crisis.

double standard and the unrestricted coinage of both metals."[1] The other three members did not favor free coinage by the United States without the concurrence of other nations. The United States took the initiative in proposing an international conference, which met in Paris on August 10, 1878, and the American delegates proposed an international agreement for the equal coinage of both metals. The majority of the delegates of the European states presented resolutions declaring "that the question of the restriction of the coinage of silver should equally be left to the discretion of each state or group of states," and that the differences of opinion which had developed "exclude the discussion of the adoption of a common ratio between the two metals."[2] The American delegates—Mr. R. E. Fenton, Mr. W. S. Groesbeck, General Francis A. Walker, and their secretary, Mr. S. Dana Horton,—filed a protest against this decision.

A second attempt to secure a bimetallic union was made in the summer of 1881 by the concurrent invitations of the American and French governments. Senator Magnin, the French Minister of Finance, presided at the opening of the conference and indicated a part of the reasons for its meeting by stating that the resolutions adopted by the majority of the European delegates in 1878 were adopted when the Dutch delegates were not present, the Italian delegates refused to be parties and the approval by other delegates was given only under reservations. The American and French delegates, through Mr. Evarts, lately Secretary of State of the United States, again urged the formation of a bimetallic agreement, and the delegates of the European states voted "that there is ground for believing that an understanding may be established between the states which have taken part in the conference; but that it is expedient to suspend its meetings." Upon their proposition, therefore, an adjourn-

[1] Reports of the Silver Commission of 1876, Sen. Rep. 703, 44th Cong., 2d. Sess., 126.

[2] International Monetary Conferrence held in Paris, in August, 1878, Sen. Ex. Doc. 58, 45th Cong., 3d Sess., 163.

ment was taken until April 12, 1882, but the conference was never reassembled.[1]

The last attempt to secure a bimetallic agreement was made at the suggestion of the United States in 1892, but the invitations were limited to the purpose of securing a larger use for silver. The British government was unwilling to enter a conference with the declared purpose of restoring the free coinage of both gold and silver and the form of the invitations was adapted by the United States to their position, in order to secure their participation in the conference. The delegates of the United States were Senator Allison of Iowa, Senator Jones of Nevada, Representative McCreary of Kentucky, Mr. Henry W. Cannon of New York, formerly Comptroller of the Currency, and Professor E. Benjamin Andrews, President of Brown University of Providence, Rhode Island. Mr. Terrell, the United States Minister at Brussels, also took part in the conference and Mr. Edward O. Leech, the Director of the Mint, was an advisory delegate. Several propositions for the purchase and coinage of silver on government account in limited quantities were submitted to the conference, but it was again found that an agreement could not be reached and an adjournment was taken on December 17, 1892, until May 30, 1893. The German delegates were unwilling to bind their government to the policy of a second meeting,[2] and the events of the winter were so little favorable to bimetallism that President Cleveland did not feel justified in seeking a reassembling of the conference.

These several efforts to restore bimetallic coinage hardly arrested for a moment the downward course of silver, and the government of British India felt that they could no longer await the distant possibilities of international action. The fall in the price of silver caused constantly increasing difficulties, because of the heavy interest charges payable in London and the diminishing value of the proceeds of taxa-

[1] Proceedings of the International Monetary Conference held in Paris in 1881; Washington, 1887; 506.

[2] International Monetary Conference, held at Brussels under the Act of August 5, 1892.—Sen. Ex. Doc. 82, 370.

tion when measured in gold. It was not merely a difficulty which weighed upon the local administration, but it affected every British officer in India who received his pay in silver rupees, originally worth about forty-eight cents, but which had been steadily declining in gold value. A remittance by bills of exchange on London to family or creditors at home meant a shrinkage of nearly fifty per cent. in the nominal value of the money received in India. These troubles led to the appointment of a special committee of able financiers by the Secretary of State for India on October 21, 1892, who submitted their report on May 31, 1893.

Rumors of the character of the report of the Indian Currency Committee began to circulate in London early in June, but their proposals still lacked the sanction of executive action. It was not until June 26, 1893, that it was officially announced that the Legislative Council of India had ordered, with the approval of the home government, the closing of the mints to the free coinage of silver on account of individuals. It was proposed at the same time to fix the exchange value of the rupee at one shilling, four pence, or the equivalent of about thirty-two cents in United States money. Such a policy had been recommended by the Committee and was supported by the experience of Holland and Austria-Hungary, which had been able by suspending the free coinage of silver to float a large mass of silver and paper currency far above the bullion value of the silver and not far below parity in gold.[1] The net imports of silver into India for the nineteen English official years ending March 31, 1893, were $704,040,907, or an annual average of $37,054,784, which had been much exceeded during the last eight years of the period. The market for nearly one-third of the annual production of the silver mines of the world was thus closed by the stroke of a pen in Downing Street.

The news of the action of the British government caused a profound sensation in the United States and increased the tendency to unreasoning panic. Secretary Carlisle had al-

[1] Report of Indian Currency Committee, Sec. 93–98.

ready, on June 22d, authorized the anticipation of the July interest on the four per cent. bonds and the Pacific Railroad six per cent. bonds, with a view to bringing the slender resources of the Treasury to the relief of the growing stringency in the money market. The Treasury was practically exhausted by the enormous purchases of bonds at a premium in the autumn of 1890 and by the abolition of the duty on sugar by the tariff act of that year, and the gold reserve was already below $100,000,000. The price of silver, which was 36 pence per ounce in London and 78 cents in New York on June 26th, tumbled to 30½ pence in London and 65 to 67 cents in New York on June 30th. The value of the bullion holdings of the government shrivelled by this change in four days by about $37,000,000, and it was evident that the United States could no longer afford to carry alone the burden of sustaining the price of silver.

President Cleveland made an earnest effort to secure the repeal of the Sherman law during the short session of the Fifty-second Congress, before taking office, as he had done in 1885 to secure the repeal of the Bland Silver Act, then in force. The House Committee on Coinage in the Fifty-second Congress had been constituted by Speaker Crisp with a majority in favor of free coinage and of continuing in force existing laws requiring Treasury purchases of silver. It was necessary, therefore, in order to bring before the House any measure repealing the Sherman law, to have it reported from another committee. Representative Andrew of Boston was one of the first to discover a way of doing this. He introduced, on December 12, 1892, a bill amending the national banking law, but containing a provision repealing the silver purchasing clause of the Act of 1890. This bill was referred under the rules to the Committee on Banking and came before the House on February 9th, by means of a special order reported by the Committee on Rules for its consideration. The order was not satisfactory in form to the advocates of repealing the Act of 1890, and its adoption, by a vote of 152 to 143, constituted their virtual defeat. The affirmative vote was given by 108 Democrats, 35 Republi-

cans, and 9 Populists and the negative vote by 105 Democrats and 38 Republicans. Several conferences were held with a view to a further effort to secure repeal or to secure a reduction of silver purchases, but no plan was framed which was acceptable to the Eastern Republicans, whose votes were necessary to make a majority for repeal. President Cleveland caused it to be understood, soon after his inauguration, that he would not summon Congress in extra session before September unless a serious crisis confronted the country. The crisis was invoked in the latter days of June, 1893, by the closing of the Indian mints and the effect upon the American currency. A meeting of the cabinet was held on June 30th, at which the increasing number of suspensions by the banks and the paralysis of business were fully discussed, and it was decided to issue a proclamation summoning Congress in extra session at noon on the 7th day of August.

The summons came none too soon and did little to stay the progress of the panic. Banking institutions, national, State, and private, were daily suspending, depositors were withdrawing their cash from the banks, and industrial enterprises were coming to a halt. Twenty-five national banks suspended in June,—a number never before exceeded in an entire year,—seventy-eight suspended in July, and thirty-eight in August.[1] The collapse of private and State banks was even more alarming. An average of about seventy suspensions per year up to the close of 1892 swelled to 415 during the first eight months of 1893, representing liabilities of $97,193,530. Banks all over the country began to refuse to pay checks except in certified or clearing-house checks, currency went to a premium, and many factories were obliged to shut down for lack of money to pay their employees. The refusal to cash checks in currency and the premium offered for it by New York brokers arrested deposits in the

[1] Eighty-four of the banks afterwards resumed business. The capital of sixty-seven national banks actually insolvent during the year ending October 31, 1893, was $11,035,000.

banks, but brought much that was in private hoards into the market.[1]

Some conception of the reduction in exchanges caused by the panic may be gathered from the shrinkage of the transactions of the New York Clearing House from $34,421,380,870 for the year ending October 1, 1893, to $24,230,145,368 for the year ending October 1, 1894. The comparison for the prosperous month of October, 1892, with the same month of 1893, showed a shrinkage in the clearing transactions of the leading cities of the United States from $5,501,901,592 to $4,043,510,662. The clearings throughout the leading cities of the country showed a shrinkage from $58,880,682,455 for the year ending September 30, 1893, which included a part of the period of panic, to $45,017,960,736 for the year ending September 30, 1894. The failures throughout the country increased from 10,270, with liabilities of $108,500,000, in 1892, to 15,560, with liabilities of $402,400,000, in 1894.

The shrinkage in money values was as marked as in the volume of exchanges. Securities which had been considered the safest ceased to pay dividends and fell rapidly in value in the hands of the holders. The Erie, the Philadelphia and Reading, the Atchison, Topeka and Santa Fe, and the Union Pacific were among the great railway systems, representing hundreds of millions of obligations, which passed into the hands of receivers. Railway earnings fell $147,390,077 during the year ending June 30, 1894, as compared with the previous year, or 12.07 per cent. of the gross earnings. Hundreds of millions of invested capital thus ceased to be productive, and those who had fancied themselves in the

[1] The surprising thing about this suspension of cash payments by some of the banks was that little public complaint was made about it. The business public seemed to recognize it as a necessary condition of the panic, although it is doubtful if it was necessary. Some of the banks continued to meet all demands for currency and nearly all paid small checks. It was estimated that $15,000,000 in currency was sold in New York during the crisis.—Alex. D. Noyes, *Political Science Quarterly*, IX., 29.

possession of an assured income from their stock holdings found their wealth turned to ashes in their hands. A crash in industrial stocks took place on May 5, 1893, but July 26th was one of the panic days on the stock exchanges. Rates for money in New York, which were normal in the morning, rose to 75 per cent. per annum before the close of business. The scarcity of money forced holders of securities to unload. Atchison general fours dropped from 71 to 66; New York, Lake Erie, and Western seconds fell from 59 to 53; Chicago gas went down from 50 to 43¾; and General Electric slumped from 47½ to 40½. The excitement in New York was so intense that it was proposed to close the Stock Exchange, but the proposition was rejected by the governors at their meeting the next day. An appeal was made to the foreign exchange houses for help and $10,000,000 in gold was engaged in London while exchange was quoted above the exporting point.

The heavy demands upon the national banks and the reduction of their coin and currency threatened early in the panic to carry their cash reserves below the limit required by law in the reserve cities. The reserves of the New York banks were close to the limit early in July and fell on August 5, $14,017,800 below it. The natural remedy for the scarcity of currency was the successful expedient of other years of panic,—the issue of clearing-house certificates. The first issues was made in Philadelphia on June 16th, but the New York banks promptly followed on June 21st, and those of Boston and Baltimore six days later. The largest amount outstanding at one time in New York was $38,280,000, from August 29th to September 6th; in Philadelphia, $10,965,000, on August 15th; in Boston, $11,445,000, from August 23d to September 1st; and in Baltimore, $1,475,000 from August 24th to September 9th. These issues, amounting with $987,000 at Pittsburg, to $63,152,000, are the only ones reported by the Comptroller of the Currency, but they only served as a lesson to the clearing houses of the country. Some form of certificate of this character was issued in nearly every considerable city

and served to greatly relieve the strain upon the ordinary circulation.

A more striking indication of the readiness of American bankers and business men to respond to the necessities of the moment was the issue of emergency paper for general circulation. The clearing-house certificates were employed only between the banks. The law imposing a ten per cent. tax upon the notes of State and private banks was supposed to stand across the path of any issues for general circulation, but the law received little attention when the absolute necessity of a circulating medium forced itself upon the country. Certificates and certified checks were issued in scores of communities where currency could not be had. They were usually guaranteed by the associated banks where there were such banks; they were issued by a single bank in even amounts where concerted action could not be obtained; and they were issued by railway companies and manufacturers where arrangements could not be made with the banks. In a few cases they were issued with the guarantee of the local authorities drawn upon some public fund. These certificates and checks proved very useful where currency was in demand for pay-rolls, were treated as cash by banks and merchants, and were promptly redeemed when the panic was over. [1]

The financial crisis of 1893 was a striking illustration of the truth that bank-note circulation plays but a trifling part, or none, in promoting crises. The national banks had been

[1] Representative John DeWitt Warner of New York, commenting upon the relations of these issues to the ten per cent. tax law, declared that "In this way, after the machinery so carefully adjusted by government had utterly failed to work, the business common sense of our people readjusted its finances; and in every part of the land business started up again, manufacture continued, the laborer received his hire, and the merchant disposed of his goods."—*Sound Currency*, Vol. II., No. 6, p. 8. These emergency issues were so entirely winked at by the government that the collections under the ten per cent. tax on bank circulation were returned by the Commissioner of Internal Revenue for the year ending June 30, 1894, as only two dollars and twenty-six cents.

contracting their secured circulation until it stood on June 1, 1893, at only $177,164,255. They had shared in the expansion of business, however, by the increase in their numbers and in their deposits. The number of national banks formed in 1890 was 307, with an aggregate capital of $36,250,000. The year 1891 showed organizations of 193 new banks, with capital of $20,700,000; 1892 showed organizations of 163 banks, with capital of $15,285,000; and 1893 had already shown 119 new organizations, with capital of $11,230,000, before the process of expansion was arrested, with the banking year only two-thirds complete. Even more remarkable was the extension of banking on deposits instead of on the capital and surplus of the banks. Bank capital increased seventy per cent. from 1870 to 1892, and the number of banks more than doubled, but individual deposits were multiplied three and one half times and rose from one-third of total liabilities in 1870 to more than one-half in 1892.

One of the defects of the operation of the national banking law, revealed anew by the crisis, was the use made of the provisions permitting the deposit in reserve cities of three-fifths of the cash reserve of the country banks and permitting the reserve banks to pay interest on such deposits. The national banks of the country on May 4, 1893, showed $174,312,119 as due from reserve agents, $121,673,794 due from national banks, and $32,681,708 due from State banks. Many banks throughout the West were obliged to suspend, because their reserves were not within ready reach. Out of a total of one hundred and fifty-eight national banks which were forced to suspend payments during the year ending October 31, 1893, eighty-six were authorized to resume business within a short time, and not one of these was east of the Ohio or north of the Potomac. This is the best proof that these Western and Southern banks would have been able to maintain their solvency if their cash reserve had been in their own custody.[1] It was also a subject of

[1] This argument is intelligently worked out by Mr. Alexander D. Noyes, "The Banks and the Panic of 1893," in *Political Science*

criticism that the banks were forbidden to make new loans when their cash reserves fell below the fixed legal limits. The Comptroller was authorized to require a bank to make good its reserve, and failing this to appoint a receiver. This power was used with moderation by Comptroller Eckels and the banks of the reserve cities increased their liquid resources by their issues of clearing-house certificates.[1]

The meeting of Congress on August 7th found the Eastern members of both political parties so strongly impressed with the serious condition of the country that they were prepared to push the repeal of the silver purchase law by the most drastic measures and by a union of forces without regard to political divisions. The message of President Cleveland, transmitted to Congress on the day following their meeting, recommended, "the prompt repeal of the provisions of the Act passed July 14, 1890, authorizing the purchase of silver bullion, and that other legislative action may put beyond all doubt or mistake the intention and the ability of the government to fulfil its pecuniary obligations in money universally recognized by all civilized countries." An agreement was reached on August 10th, between the supporters and opponents of the President, that debate should begin the next day and that the vote on a repealing bill should be taken on August 28th. Mr. Wilson of West Virginia, the recognized leader of the Democratic majority of the House, introduced a repealing bill early the next morning. The silver men, in accordance with their pledges to their opponents, made no attempt to interpose dilatory tactics and the roll was called on the passage of the bill on the 28th of August.

The votes given upon this day showed the largest majority against the silver standard given for many years in the House of Representatives. The first vote was taken upon a motion of Representative Bland of Missouri, for the opening of the mints of the United States to the free coinage

Quarterly, IX., 12. It is not to be inferred that deposits in reserve cities should be cut off entirely, but simply that they should be confined within more prudent limits.

[1] Report on the Finances, 1893, 356.

of silver at the ratio of sixteen to one. The vote was 125 in the affirmative and 226 in the negative,—a majority of 101 against the proposition. The intense interest taken in the issue and the demand from the country that every member should be accounted for is indicated by the size of the vote, which included every living member of the House except two,—a sick member from New York who was paired in favor of repeal with a South Carolina silver member. The next vote was taken upon free coinage at the ratio of seventeen to one, which was rejected, 101 to 241. Free coinage at the ratio of eighteen to one was rejected, 103 to 240; free coinage at the ratio of nineteen to one was rejected, 104 to 238; free coinage at the ratio of twenty to one was rejected, 122 to 222. The next motion of Mr. Bland's was to revive the Act of February 28, 1878, requiring the monthly purchase of not less than $2,000,000 worth of silver bullion and its coinage into standard silver dollars. The silver men rallied their greatest strength upon this proposition, which they represented as a compromise, but Mr. Bland's motion was rejected, 136 to 213. The roll was then called upon the repealing bill of Mr. Wilson and it was passed, 239 to 109,—a clear majority of 130 votes. The affirmative vote was cast by 138 Democrats and 101 Republicans; the negative vote was cast by 73 Democrats, 25 Republicans, and 11 Populists and Independents.

The indications of favorable action in the Senate, where the supporters of silver were strongest, were greatly strengthened when the Committee on Finance voted, on August 18th, to report a repealing bill, similar in its effects to the bill which was before the House, but containing some declaratory matter in favor of maintaining the parity of gold and silver. A careful canvass, during the progress of the debate, revealed the conversion to the repeal side of enough administration Democrats and moderate Republicans to make a majority of eleven for repeal. The existence of this majority seemed for a time, however, to be of little avail against the cumbersome rules of the Senate. The silver Senators, by persistent dilatory tactics, brought the Senate

at least twice close to the verge of surrender to their wishes. The last and most serious occasion was after the failure of the attempt to tire out the silver leaders by a night session. The Senate went into continuous session on the evening of October 11th, but the Populist Senator, Allen of Nebraska, held the floor continuously for fifteen hours, and the attempt to maintain a quorum of repeal members broke down at half-past one o'clock on the morning of October 13th. Senator Gorman of Maryland, who had never expressed any confidence of getting a vote on repeal, was one of the promoters of the compromise then proposed, and every Democratic Senator but four signed an agreement to support it. The President refused to countenance compromise in a statement given out on Sunday night, October 22d, and the renewed firmness of the friends of repeal forced the silver men three days later to lay down their arms and admit that they could not postpone indefinitely a vote on the bill. The repeal bill passed the Senate on October 30th, by a vote of 43 to 32, with five pairs; two days later, on November 1st, the Senate amendments to the form of the bill were concurred in by the House, and the bill was approved by the President.[1]

The acute stage of the crisis was over before the approval of the silver repeal bill by the President, but the expected revival of activity did not follow on the heels of repeal. Confidence in American credit abroad had been too severely shaken and the unfavorable conditions created by the Sherman law were still felt with too much force for business to resume at once its wonted activity. The history of former financial crises was repeated in the accumulation of idle capital in the banks in the form of deposits, the swelling of the cash reserves, and the reduction of commercial loans.

[1] The writer by a rather curious coincidence, predicted in the *Journal of Commerce and Commercial Bulletin* on July 6th, and in the *Springfield Republican* on July 10, 1893, the exact date on which the repeal bill would become law. "The Sherman law cannot be repealed before November 1st," was the language used in the *Republican*, and the course of events under the rules of the two houses of Congress was outlined almost exactly as they afterwards occurred.

The following table shows the state of the loans, the specie reserve, and the individual deposits of the national banks at various dates before the crisis and during the period of depression which followed, according to the reports to the Comptroller of the Currency :

DATE.	LOANS AND DISCOUNTS.	SPECIE RESERVE.	INDIVIDUAL DEPOSITS.
May 4, 1893	$2,161,401,858	$207,222,141	$1,749,930,817
July 12, 1893	2,020,483,671	186,761,173	1,556,761,230
October 3, 1893	1,843,634,167	224,703,860	1,451,124,330
December 19, 1893	1,871,574,769	251,253,648	1,539,399,795
February 28, 1894	1,872,402,605	256,166,585	1,586,800,444
May 4, 1894	1,926,686,824	259,941,923	1,670,958,769
July 18, 1894	1,944,441,315	250,670,652	1,677,801,200
October 2, 1894	2,007,122,191	237,250,654	1,728,418,819
December 19, 1894	1,191,913,123	218,041,222	1,695,489,346
March 5, 1895	1,965,375,368	220,931,641	1,667,843,286
May 7, 1895	1,989,411,201	218,646,599	1,690,961,299
July 11, 1895	2,016,639,535	214,427,194	1,736,022,006
September 28, 1895	2,059,408,402	196,237,311	1,701,653,521

These figures show the gradual reduction and slow recovery of the loans and discounts, which afford the best measure of business activity. The individual deposits suffered at first, but began to recover, as timid capital was withdrawn from active investment. The accumulations of idle capital were largest in New York and other cities of the East, because less capital had been destroyed there by bad investments and less was needed to support consumption which was no longer supplied by current earnings. The partial restoration of confidence in the banks, unaccompanied by sufficient general confidence to promote new business enterprises, transformed the scarcity of currency which prevailed at the acute state of the panic into plethora, which there was no means of relieving except by the export of gold. Gold for export had been furnished up to 1892 by the banks of New York city, and the banks and the government mutually paid gold and gold certificates in the settlement of their balances at the New York Clearing House. The settlement of these balances in gold was practically sus-

pended by the Treasury in the summer of 1892. The banks were obliged to withhold gold from their customers for the payment of custom duties and to send them to the Treasury for gold for export.

The combined effects of the loss of gold income, the reduction of receipts, the plethora of government paper currency, and the continued withdrawal of foreign capital was to compel four issues of bonds, aggregating $262,315,400 in principal and $293,000,000 in net proceeds to the Treasury, during 1894, 1895, and 1896. The most potent cause of these losses was the withdrawal of foreign capital, but this withdrawal was itself stimulated by the accumulation of idle currency, and the distrust of the financial policy of the United States which was invoked by the reduction of the gold reserve. The operation of the legal tender currency and of the Act of 1878, forbidding its cancellation when redeemed, was to expose the Treasury to persistent raids for gold, against which it had no means of protection through the interest rate, the charging of a premium, or the control of the foreign exchanges. The very gold paid into the Treasury for bonds sold to replenish the reserve, was obtained in large measure by the presentation of legal tender notes at the New York sub-Treasury for redemption.

The bids for the first issue of $50,000,000 in five per cent. ten year bonds were opened on February 1, 1894, and the reserve was raised on February 28th, to $106,527,068. Gold exports from the United States set in heavily again in April, 1894, and were not arrested until the beginning of the outward movement of the crops in August. The net exports of gold from the United States, after deducting imports, were $9,402,110 in April, $23,124,058 in May, $22,376,872 in June, $12,823,572 in July, and $1,935,303 in August, 1894, when the tide turned slightly in the other direction. The respite was but a short one and bids for another block of $50,000,000 in five per cent. ten year bonds were opened November 24, 1894.[1] The reserve was restored from $58,-

[1] The net proceeds of the first loan were $58,660,917, and of the second $58,538,500.—*Finance Report*, 1894, LXIX-LXX.

875,317 on September 29th, to $106,821,428 on December 10th; but the demand for the redemption of notes in gold during the next two months surpassed all previous experience and carried the reserve down to $44,705,967 on January 31, 1895. The redemptions of November were $7,799,747 and those of December $31,907,221. There was a slackening of the pressure during the early days of January, but it set in again with renewed violence during the last ten days of the month and drove the Treasury to the verge of the suspension of gold payments. The single day of January 25, 1895, showed redemptions of $7,156,046, and the evening of Saturday, February 2d, arrived with only $9,700,000 in gold coin available in the New York sub-Treasury. Even this was obtained by trenching upon the fund held for the redemption of gold certificates. Panic was seizing the business community and a single New York bank reported to Assistant Secretary Curtis that on January 30th they received over one hundred and fifty requests for gold coin, most of it evidently for hoarding.[1]

President Cleveland recommended the retirement of the legal tender notes and the substitution of a banking currency in his annual message to Congress in December, but the House of Representatives on January 9, 1895, refused to consider the bill reported in pursuance of this recommendation. The President on January 28th sent a special message to Congress, asking that he be given authority to retire the greenbacks and to issue bonds under more favorable conditions than those authorized by existing law. A bill to carry out his recommendations was introduced by Chairman

[1] Distrust of the security of United States notes or the pressure of the excessive paper currency produced a very different attitude on the part of the public towards the gold reserve after the passage of the Sherman law from that which prevailed before. The paper money presented to the Treasury for redemption in gold was $7,976,698 during the fiscal year 1879, the first six months after resumption, and declined in 1882 as low as $40,000. The largest redemptions between 1879 and 1891 were $6,863,699 in 1886. The redemptions in 1891 were $5,986,070; in 1892, $9,125,842; in 1893, $102,100,345; in 1894, $84,802,150; and in 1895, $117,354,178.

Springer of the Banking Committee and reported by him to the House two days later. The bill authorized the issue of three per cent. bonds, redeemable after ten days at the pleasure of the government; the cancellation of the greenbacks received in payment for the bonds, to the amount of new circulation issued; and the increase of national bank circulation to the par value of bonds deposited as security. This bill was defeated, on January 7th, by a vote of 135 to 162.

The eighth day of February, 1895, was marked by the delivery to Congress of a special message from President Cleveland, describing one of the most notable transactions of modern finance. The President announced the completion of a contract for the purchase by the government of 3,500,000 ounces of standard gold coin, by the delivery of about $62,400,000 in four per cent. coin bonds, redeemable after thirty years.[1] The purchasers of the bonds were Messrs. August Belmont and Co., on behalf of themselves, and Messrs. N. M. Rothschild and Sons, of London, and Messrs. J. P. Morgan and Co., on behalf of themselves and Messrs. J. S. Morgan and Co. of London. The contract was witnessed by Assistant Secretary William E. Curtis, who had much to do with bringing it to a successful completion, and by Mr. Francis Lynde Stetson of New York. There was an alternative clause, reserving to the Secretary of the Treasury the right, in case he should receive authority from Congress within ten days, to substitute three per cent. bonds specifically payable in gold coin for the coin bonds authorized by existing law. The effect of this substitution, if the gold bonds were accepted at par, as the contract provided, would have been, according to the message of the President, to save the United States in interest charges $539,159 per year, or $16,174,770 during the thirty years fixed as the term of the bonds. A bill to authorize this substitution of gold bonds was reported by Chairman Wilson of the Ways and

[1] The actual transactions under the contract were the delivery of $65,116,244 in gold for $62,315,400 in bonds.—*Finance Report*, 1895, LVI.

Means Committee of the House on February 13, 1895, but was defeated in the House the next day by a vote of 120 to 167, and the contract was left in force according to its original terms.

The peculiar feature of this contract for the exchange of bonds for gold lay in the provision that the purchasers of the bonds, "as far as lies in their power, will exert all financial influence and will make all legitimate efforts to protect the Treasury of the United States against the withdrawal of gold pending the complete performance of this contract." The fulfilment of this pledge was accomplished through the control over the foreign exchanges which was exercised by the firms which purchased the bonds. They brought into their syndicate the leading gold shipping houses, and foreign bills of exchange were placed upon the market for several months in just sufficient quantities to meet the current demand. The syndicate by this process created debts in Europe which it was necessary to cover at some time by the purchase of exchange or the shipment of gold. They guarded in a measure against possible losses by keeping the rate for the bills which they sold considerably above the gold shipping point. They thus, in effect, created a corner in foreign exchange and imposed the cost of their operations upon the purchasers of foreign bills. This method of controlling exchange operated with wonderful success all through the spring and up to the closing days of July. The tide of gold exports, which rose to $24,698,489 in the month of January, was turned into net imports by the operations of the syndicate in bringing gold from Europe. February showed net imports of $4,067,003; March, net imports of $4,120,290; April, net imports of $2,029,761; May, net imof $3,271,193; and June, net imports of $1,963,750. The effect upon the treasury was equally striking. The redemptions of United States legal tender notes in gold, which had been $45,117,738 in January, were reduced to $5,560,952 in February, $1,089,085 in March, $1,017,571 in April, $1,166,472 in May, and $1,239,287 in June.

The essential purpose of the contract, in spite of criticisms

to which it was justly subject, was to afford a breathing spell to the country for the restoration of confidence in the monetary standard and in the business future. The period of business depression beginning in 1893 had lasted long enough to exhaust idle stocks of goods, to accumulate capital in the banks, and to prepare the business community for a new period of activity if confidence could be restored. Mr. J. Pierpont Morgan, the eminent financier who was the leading spirit in the arrangement, would probably have made no attempt to restore confidence and business activity by similar methods in the spring of 1893 or of 1894, but he counted upon the probabilities of success in such an undertaking in 1895, and events partially justified his judgment. The loans and discounts of the national banks of the City of New York increased from $332,069,999 on March 5, 1895, to $363,848,573 on September 28, 1895, while the loans and discounts of all the national banks of the country advanced in the same interval from $1,965,375,368 to $2,059,408,402. The imports for the calendar year 1895 were $801,663,490, an increase of $125,000,000 over 1894, and only $39,000,000 less than in the prosperous year 1892. Receipts for postage, an unfailing index of business conditions, increased in every quarter of 1895 over the corresponding quarter of 1894, and reached for the concluding quarter of the year a total of $20,517,014, the largest volume of business ever recorded.

The essential defects of the policy of the syndicate contract were its failure to diminish the redundant volume of currency, the stimulus thus afforded to imports over exports, and the artificial nature of the attempt to corner the exchange market. This attempt practically broke down towards the close of July. A leading coffee firm which had payments to make in Europe found that they could be made cheaper by the shipment of gold drawn from the Treasury than by the purchase of exchange at the rates fixed by the syndicate. One of the syndicate firms was also compelled to ship gold withdrawn from the Treasury, in order to cover the bills of exchange which they had sold. The syndicate had been released from a part of the obligation to bring half the gold

in payment for the bonds from abroad, and had completed their deliveries under the contract on June 24, 1895. Members of the syndicate still held considerable quantities of gold, and the first exports were made up by voluntary deposits of this gold in the Treasury, amounting up to September 11, 1895, to $16,127,432. These deposits several times restored the reserve to $100,000,000, when it was on the point of falling below that amount, but the reserve slowly travelled downward from $107,512,362 at the end of June to $92,943,179 at the end of October.

The loss of control over the exchange market practically terminated the efforts of the syndicate to maintain the reserve, in spite of their voluntary gold deposits. The gold obtained for shipment continued to be drawn almost exclusively from the Treasury, the net exports were $13,468,188 in November and $14,170,899 in December, and the gold reserve fell to $63,262,268 on December 31, 1895. President Cleveland in the meantime delivered to Congress on December 3d, his annual message, laying special stress upon the importance of retiring, by means of a bond issue, the legal tender notes, which were presented over and over again to the Treasury for redemption and were required by the Act of May 31, 1878, to be "re-issued and paid out again and kept in circulation." Congress gave no indication of compliance with this recommendation, and the raid upon the gold reserve increased in intensity after the delivery of the special message of the President upon the encroachments of Great Britain upon the Venezuelan boundary. The possibility of war between Great Britain and the United States led English investors to unload American securities, caused large withdrawals of gold from the Treasury for export, and brought the country to the verge of the suspension of gold payments. The President, on December 20th, called the attention of Congress in a special message to the serious financial condition of the country and urged that they should not take a recess for the holidays without taking some step for the protection of the public credit. An effort was made by Congress to pass some legislation, but it was not satis-

factory at any time to the administration, because provision was not made for the issue of bonds specifically payable in gold nor for the retirement of legal tender notes. It soon appeared that the Senate and House could not agree upon any measure between themselves, and the President and Secretary of the Treasury determined upon another issue of bonds under the existing law.

A public call for subscriptions to $100,000,000 of four per cent. coin bonds, dated February 1, 1895, and payable at the pleasure of the United States after thirty years, was issued by Secretary Carlisle on January 5, 1896. There was some doubt at first among financiers whether the subscriptions from responsible holders of gold would be sufficient to permanently restore the gold reserve. Mr. J. Pierpont Morgan had been organizing a syndicate, in the hope of making a contract with the government similar to that of 1895, and the fact that he intended to obtain gold for the execution of his part of the contract from outside the Treasury gave the plan, in the opinion of many financiers, an advantage over a popular loan. The response to the call of Secretary Carlisle, however, when the bids were opened on February 5th, was such as to dissipate such fears and to materially strengthen the public credit. The number of subscriptions of an apparently *bona fide* character was four thousand six hundred and forty, and the amount was $568,269,850. A syndicate headed by Mr. Morgan subscribed for the entire amount at 110.6877. It was found that there were subscriptions for $66,788,650 at higher figures, so that Mr. Morgan's syndicate were allotted only the remainder of the $100,000,000. Subsequent defaults on the part of some of the subscribers raised Mr. Morgan's allotment to about $38,000,000 and made the net proceeds of the loan about $111,250,000. The gold reserve of the Treasury was rapidly increased by the deposit of gold in payment for the bonds and rose on March 17, 1896, to $127,862,644. The loan appeared to afford some of the advantages in restoring business confidence afforded by the syndicate contract of 1895. Business showed increased activity, and net exports of gold, to the amount of $13,468,-

188 in November and $14,170,899 in December, were reduced to $198,586 in January and transformed into net imports of $9,375,389 in February, 1896.

The crisis in Australia in 1893 was one of those peculiar to new countries. The future had been too rapidly discounted, speculation in land had been carried beyond the possibility of the immediate development of the country and an enormous debt had been created for public works. Competition in banking had been carried to such an extreme that nearly every little community supported branches of all the leading banks, and obtained excessive loans on property which could not be converted into quick assets. Not content with loaning their own funds in this way, the Australian banks established agencies all over the United Kingdom, with some local solicitor or stock broker as agent, and paid commissions to obtain deposits. When the crisis broke out in January 1893, the British deposits in the Australian banks were about one-third of the total deposits of £153,000,000. Foreign money had poured into Australia under the conviction among British investors that investments among those of their own blood were safer than among the South American republics or the decrepit nations of Eastern and Southern Europe.

This easy accession of riches came to be counted by the Australians as part and parcel of their own accumulations. A circular issued on behalf of a public loan for the colony of Victoria in 1892 counted up the wealth of the people at £440,000,000 or at the rate of nearly £400 for each of the 1,140,000 inhabitants. This valuation was more than fifty per cent. greater per capita than that of Great Britain, after centuries of accumulation, but it was made up by appraising unsettled lands at £2 per acre which could not be sold today for £1 and by a similar process of inflation of bank credits and personal wealth.[1] The City of Melbourne, with its population of 500,000, was extended on the maps of the land speculators to limits which would have afforded ample

[1] Raffalovich, *Le Marché Financier en 1893–94*, 305.

accommodations for a city with twice the population of London. The feeling of affluence which such figures caused had encouraged the creation of a public debt of about £34 per head, almost exactly twice the enormous public debt of the United Kingdom.

Stubborn facts did not bear out these inflated valuations and the adoption of the protective policy in a country where manufacturing had hardly been born added to the fetters upon consumption, whatever might be expected from its final results in developing native industries. The revision of the tariff in 1892 was made with the avowed purpose of obtaining additional revenue to meet the charges on the foreign debt, but its results were to reduce the customs receipts for the fiscal year 1893 by about £250,000. Warnings against the land boom were given several years before the crisis of 1893, but many of the banks had plunged in so deep and tied up so large a proportion of their assets in landed security that they dared not take a backward step. Advances once made on land were increased in proportion to the fictitious value reached by speculation, the discount on the added loan was deducted from the new advance to the borrower, and this actual increase in the risk of the bank was carried to the fictitious account of earnings and profit.[1]

A large proportion of the British deposits which had been secured through agents were owned in Scotland and fell due on the half yearly term days. Every half year represented a critical point in Australian banking and none looked more critical as it drew near than the Whitsunday term of 1893. The danger was so threatening, that some of the banks would be compelled to suspend, by demands from Scotland, that Australian depositors began to withdraw their accounts and thus brought about the collapse which might otherwise have been again postponed. The signal of the actual crash came on January 29th, when the Federal Bank of Melbourne failed. It was a new institution, with limited capital, long looked upon with distrust by the older banks, and a strong

[1] Sydney J. Murray, London *Bankers' Magazine*, Oct., 1895, LX., 479.

effort was made to create the impression that the failure had simply cleared the air and left the older institutions stronger than before. The public refused to accept this view of the case and gradually began to withdraw their deposits from all the banks. Notices of withdrawal poured in from Great Britain, and on April 4th the Commercial Bank of Australasia closed its doors, with deposits of £12,044,000. The English and Australian Bank, with deposits of £5,795,000 and ninety-one branches, stopped payment on April 12th, and the London Chartered Bank, with deposits of £6,588,000 and fifty-eight branches, closed its doors during the next week. The government proclaimed a five days' holiday early in May, in the hope that public excitement would subside while the banks were enjoying a breathing spell. But banks continued to go down, and when the last failure occurred on May 17th, fourteen institutions had failed with aggregate deposits of £85,000,000, including £26,000,000 owed in Great Britain.

Twelve banks, with deposits before the panic of £71,000,000, succeeded in weathering the storm and did much to restore confidence by their refusal to avail themselves of some of the devices of the weaker institutions. The government of New South Wales made bank-notes a legal tender for six months, which enabled the banks, without increasing circulation more than ten per cent., to come to the relief of commerce by liberal loans. The surplus of loanable capital in Europe brought some relief, when the substantial character of the assets of the stronger banks become known, and plans of reconstruction were soon set in motion.[1] There is still some apprehension as to the ability of the banks to meet their extended obligations at maturity, and the belief is held by careful observers of Australian affairs that the reduction of competing branches of the banks has not proceeded far enough. The era of inflation has, however, been brought to an end, and the great resources of Australia seem likely to permit a gradual recovery of her real prosperity, if not of the inflated values of former times.

[1] London *Bankers' Magazine*, May, 1895, LIX., 715.

CHAPTER XXIII.

THE ADVANTAGES OF A BANKING CURRENCY.

It is Created for Carrying on Business and is Subject to Business Conditions—The Volume of Exchanges through the Banks and Clearing Houses—Superiority of Bank-notes over Government Paper Money in Convenience, the Promotion of Banking Facilities, and Stability—The Importance of Large Liquid Assets in Maintaining Redemption on Demand.

THE inherent advantage of a currency issued by well regulated banks is its adaptation to business needs. It is the outgrowth of the relations of business men with each other and, where its essential character has not been too much modified by repressive laws, it represents the evolution of the simplest and best methods of making commercial exchanges. Being the growth and creature of business transactions, its adaptability to them is more nearly perfect, of necessity, than other systems originated for other purposes and only incidentally shaped to accommodate such needs. It is of prime importance that there should be a fixed metallic standard of value, just as it is of importance that there should be a fixed official length for the meter or yard-stick. The standard being fixed, the duty of the state is done and it should be left for the business community to conduct its transactions, so long as they are measured by the standard, by the means which it finds most convenient. These means, the business community has decreed, are found in the various forms of commercial paper. The great development of modern credit has made bank-notes only the small change in such transactions, but they are of supreme importance in giving credit birth where it is unknown and

are still the essential tools of the retail trade which makes possible the greater commerce.

The essential advantages of a banking currency may be summarized under these heads :

1. Economy and convenience in making payments.
2. The adjustment of the volume of currency to business conditions.
3. The promotion of banking facilities and of the use of instruments of credit.
4. The adherence to a fixed metallic standard of value.

I. The economy of payment by means of paper credit was understood in remote antiquity, when bills of exchange occasionally took the place of physical transfers of silver and gold. In more modern times, the application of the same economy to domestic transactions has given birth to checks, domestic bills of exchange, bank-notes, bank credits, and clearings. Every such transaction which dispenses with metallic money, without impairing the safety of the standard, saves to the community the capital which would otherwise be employed in the mere mechanism of exchange and releases it for the active service of production and reproduction. The economic effects of this saving have been set forth by Adam Smith in a passage which has become classic :[1]

> The gold and silver money which circulates in any country, and by means of which the produce of its land and labor is annually circulated and distributed to the proper consumers, is, in the same manner as the ready money of the dealer, all dead stock. It is a very valuable part of the capital of the country, which produces nothing to the country. The judicious operations of banking, by substituting paper in the room of a great part of this gold and silver, enable the country to convert a great part of this dead stock into active and productive stock ; into stock which produces something to the country. The gold and silver money which circulates in any country may very properly be compared to a highway, which, while it circulates and carries to market all the grass and corn of the country, produces itself not a single pile of either. The judicious operations of banking, by providing, if I may be allowed so violent a metaphor, a sort

[1] *Wealth of Nations*, B. II., Ch. ii. (I., 321–22).

of wagon-way through the air, enable the country to convert, as it were, a great part of its highways into good pastures and corn-fields, and thereby to increase very considerably the annual produce of its land and labor.

The extent in our time of this substitution of paper credit for metallic money, without hampering the operations of trade, is as great a marvel in its way as the development of the power of steam or electricity. The volume of metallic money has grown from year to year, until the amount in use in the world is computed at over $8,000,000,000;[1] but the expansion in the volume of money has followed with but halting steps the growth in the volume of commercial transactions and the development of the use of credit in carrying them on. An estimate of the aggregate of the world's transactions would be an idle undertaking. The most that is possible is a record of the balances which pass through the banks and clearing houses of a few commercial centres. The use of circulating notes has become but a small part of these great transactions, but still remains under many conditions an important part. Banks now do business largely through the power to grant credits on their books, which is derived from their deposits. The total banking power of the world, including capital and deposits, is calculated by Mr. Muhleman, the able Deputy Assistant Treasurer of

[1] The economy in the substitution of paper money and bank-notes for coin has become a factor relatively so small in comparison with the economy of other forms of credit that it is not necessary to dwell upon it at length; but the development of the other forms of credit is often promoted, as will appear later, by the power to issue bank-notes. The gold in use in the world as money in 1895, according to the report of the Director of the United States Mint, was $4,086,800,000 and the silver, at the coining value, was $4,070,500,000. The cost of maintaining £95,000,000 in gold, silver, and copper in circulation in Great Britain is estimated by Mr. W. Stanley Jevons at £2,972,000 ($14,500,000) annually, of which £2,850,000 is for interest at three per cent. *Investigations in Currency and Finance*, 296. The cost of maintaining the currency of the United States, if the present volume of about $1,600,000,000 were exclusively metallic, would be about $45,000,000 annually; and the annual cost of maintaining the actual gold and silver circulation of the world is about $240,000,000.

the United States at New York, at £3,915,000,000, or $19,000,000,000, distributed as follows :[1]

Europe,	£2,200,000,000
Asia,	150,000,000
Africa,	50,000,000
Oceanica,	175,000,000
North America,	1,200,000,000
South America,	140,000,000
	£3,915,000,000

The banking resources of the banks of the United Kingdom of Great Britain and Ireland alone are nearly £1,000,000,000, and such resources attained in the United States in 1895 the even greater total of $6,703,544,084.[2] This vast banking power, moreover, represents only partially the capacity of the banks of the world for conducting exchanges. The exchanges through the clearing houses in the great commercial countries represent annually many times their capital, or circulation, or deposits at any fixed date, and more than the entire net earnings of the people. The London Clearing House was in operation as early as 1773, but the universal use of the clearing system is a development of the last half century. The private bankers retained exclusive control of the London Clearing House until 1854, when the London and Westminster and other leading joint stock banks were permitted to share in its advantages.[3] The Bank of England was not admitted until 1864, and even at the pres-

[1] *Monetary Systems of the World*, 160. This calculation is based in part upon an estimate of Mr. Mulhall, the English statistician, in 1889, but the estimate is enlarged to correspond to the more recent date and to known omissions in his figures.

[2] For the United Kingdom, see p. 135. The figures for the United States include the aggregate capital, surplus, undivided profits, and individual deposits of national banks on July 11, 1895, and of State, stock savings, and private banks, and loan and trust companies at date of latest report.—Comptroller's Report, 1895, 512.

[3] Prof. MacLeod computes that the admission of the joint stock banks released them from keeping £500,000 in currency almost constantly on hand, and made that amount available for general circulation.—*Theory and Practice of Banking*, II., 183–84.

ent time some of the large Scotch banks do their business indirectly, through the agency of another bank.

The Paris Clearing House is composed of eleven banking houses and was not organized on its present basis until 1872. The Vienna Clearing House, with a dozen leading banking houses grouped around the Imperial Bank of Austria-Hungary, was organized in the same year, but several of the private banks had adjusted their compensations between themselves as early as 1864. Clearing houses were established in Italy by legal decree of May 19, 1881, at Rome, Milan, Geneva, Bologna, Florence, and Catana. Cologne and Stuttgart have each possessed a clearing house since 1882, and one was formed at Berlin in 1883, with the Imperial Bank as its centre. No clearing system seems to have existed in Germany prior to this date, but the Imperial Bank, the Check Bank of Hamburg, and several others, practised the use of transfer checks upon a large scale, and clearing houses are now in operation at Hamburg, Bremen, Leipsic, Breslau, and Dresden.[1] The operations through the London Clearing House were £954,000,000 in 1839, and £1,900,000,000 in 1857.[2] Their magnitude in recent years is indicated in the following table:

YEAR.	ON STOCK EXCHANGE SETTLING DAYS.	PER CENT. OF TOTAL.	TOTALS FOR THE YEAR.
1868	£ 523,349,000	15.3	£3,425,185,000
1872	1,015,959,000	17.2	5,916,452,000
1874	1,010,456,000	17.0	5,936,772,000
1876	761,091,000	15.4	4,963,480,000
1878	795,443,000	15.9	4,992,398,000
1880	1,151,867,000	19.8	5,794,238,000
1882	1,228,916,000	19.7	6,221,206,000
1884	960,623,000	16.6	5,798,555,000
1886	1,198,557,000	20.3	5,901,925,000
1888	1,252,466,000	18.9	6,916,133,000
1890	1,416,543,000	18.1	7,801,048,000
1891	1,067,403,000	15.5	6,847,506,000
1892	1,022,764,000	15.7	6,481,562,000
1893	1,002,664,000	15.4	6,478,013,900
1894	964,455,000	15.2	6,337,222,000
1895	1,304,679,000	17.1	7,592,886,000

[1] Arnauné, 382–84.

[2] The largest amount of bank-notes used in 1839 in one day for the

The clearings at Paris were 1,602,584,727 francs in the year ending March 31, 1873; 3,222,745,255 francs in 1880; 4,142,562,483 francs in 1885; 5,140,959,989 francs in 1890; 6,003,883,202 francs in 1891; and 5,379,348,428 francs in 1894. These figures, however, give an incomplete idea of the banking business done in Paris. A great central bank operates in some measure as a clearing house in itself, and this is more notably the case with the Bank of France, with its comparatively feeble rivals, than with the Bank of England, surrounded by the great stock banks and private banks. The last report of the Board of Regents of the Bank of France shows the transactions for 1894, including deposits of bills and currency and transfers by checks on the central bank, to have been 61,500,196,400 francs ($12,000,000,000), of which 45,150,142,500 francs was in checks, 15,098,022,600 in bank bills, and 1,252,031,300 francs in specie. Thus three times the net income of all Frenchmen passes annually through the bank in the form of currency or credits. The regents remark that, "as every transfer represents a payment and a receipt, there is a movement of funds of ninety milliards effected without the displacement of bills or specie," and they add that they have a right to say that the bank "fulfils in France, without cost to its clients and without profit for itself, the functions of the English Clearing House."[1]

The Bank of France has kept for many years an exact account of its daily receipts, which indicates not only the

payment of balances was £593,900. The balances settled in 1879-80 ran as high as £5,334,000, but settlements had ceased since 1854 to be made in notes, or they would have absorbed one-fifth of the circulation of the Bank of England.—London *Bankers' Magazine*, Feb., 1896, LXI., 253.

[1] *Assemblée Générale de la Banque de France, du 31 Janvier, 1895*, p. 7. The fact that money transfers are so much in excess of incomes is due to the fact that the incomes of traders represent a much larger volume of transactions than their profits, which figure as net income. The estimates of M. Leroy-Beaulieu and other authorities put the net incomes of Frenchmen at 20,000,000,000 francs ($4,000,000,000), equivalent to about $107 per capita, or $535 for a family of five.—*La Science des Finances*, I., 380.

vast aggregate of its transactions, but the comparatively small part which is played in them by coin and bank-notes. The figures for representative years have been as follows:

YEAR.	SPECIE.	NOTES.	TRANSFERS OR CHECKS.	TOTAL.
		(In millions of francs.)		
1817	534.9	7,140.9	....	7,675.8
1820	248.6	6,406.8	....	6,655.4
1830	624.4	4,882.1	2,382.2	7,888.7
1840	955.9	4,150.1	3,281.4	8,387.4
1850	2,327.7	6,962.1	3,499.3	12,789.1
1860	6,629.1	15,411.0	11,488.4	33,528.5
1870	6,458.1	23,496.3	19,037.2	48,991.6
1880	5,323.3	32,095.1	32,713.5	70,131.9
1890	3,098.8	36,437.9	43,330.7	82,867.5
1891	3,002.2	37,990.1	48,745.0	89,737.7
1892	2,712.1	35,357.2	37,451.6	75,520.8
1893	3,168.5	33,521.5	38,090.5	74,780.6
1894	2,727.5	34,921.6	46,170.0	83,819.2

The exchanges of the clearing houses in the United States, although far from comprehending the transactions of all the banks, have several times been in excess of $50,000,000,000, or more than the net annual earnings of the people. Clearing houses have been established from year to year in the smaller cities of the country, until there are in 1896 about seventy-five as compared with forty in 1888, but the clearings of the new institutions are not large enough to greatly impair the value of the comparisons for the various years. The total clearings for the year ending September 30, 1888, were $48,750,886,813; for 1889, $54,494,754,586; for 1890, $59,882,477,513; for 1891, $56,803,253,957; for 1892, $60,883,572,438; for 1893, $58,880,682,455; for 1894, $45,028,496,746; and for 1895, $51,111,591,928. The transactions of the New York Clearing House have been carefully recorded since 1854 and the following figures show the progressive increase in representative years:

YEAR.	CLEARINGS.	BALANCES PAID IN MONEY.	PER CENT. OF BALANCES TO CLEARINGS.
1854	$5,750,455,987	$297,411,494	5.2
1860	7,231,143,057	380,693,438	5.3
1865	26,032,384,342	1,035,765,108	4.0
1869	37,407,028,987	1,120,318,308	3.0
1870	27,804,539,406	1,036,484,822	3.7
1873	35,461,052,826	1,474,508,025	4.1
1876	21,597,274,247	1,295,042,029	5.9
1879	25,178,770,691	1,400,111,063	5.6
1880	37,182,128,621	1,516,538,631	4.1
1881	48,565,818,212	1,776,018,162	3.5
1885	25,250,791,440	1,295,355,252	5.1
1890	37,660,686,572	1,753,040,145	4.7
1891	34,053,698,770	1,584,635,500	4.6
1892	36,279,905,236	1,861,500,575	5.1
1893	34,421,380,870	1,696,207,176	4.9
1894	24,230,145,368	1,585,241,634	6.5
1895	28,264,379,126	1,896,574,349	6.7

Several investigations during the last two decades have shown that more than ninety per cent. of the transactions through banks at the leading commercial cities are concluded by means of checks, bills of exchange and other instruments of credit, exclusive of bank-notes. The last investigation of this sort in the United States was made by the Comptroller of the Currency in 1892 and called upon national banks to separate the various items of their receipts on September 15th of that year. The result obtained was as follows:

LOCATION OF BANKS.	NO. OF BANKS.	TOTAL RECEIPTS.	PER CENT.		
			COIN.	PAPER CURRENCY.	CHECKS, DRAFTS, ETC.
New York,	48	$130,976,963	0.11	7.53	92.36
Other reserve cities,	281	116,514,324	0.82	6.44	92.74
Banks elsewhere,	3,144	83,713,926	3.80	11.29	84.91
United States,	3,473	$331,205,213	1.29	8.10	90.61

While the bewildering aggregates of clearing operations swell from year to year with the increase in business transactions, an opposite effect has been produced upon the clear-

ing house records by the creation of stock exchange clearing houses for the settlement of transactions in negotiable securities. The first official stock exchange clearing house was founded at Frankfort in May, 1867, and it was found that settlements involving $250,000,000 in securities could be made by the payment of $5,000,000 in currency. The primary feature of the stock exchange clearing houses is the setting off of sales of stock by certain brokers against purchases of the same stock by other brokers, so that the final balances only are delivered by the clearing houses. Several of the stock exchange clearing houses go further, however, and settle the entire money balances between the brokers. The Berlin exchange adopted the clearing system in 1869, the Hamburg exchange in 1870, that of Vienna in 1873, and that of London in 1876. The peculiar organization of the Paris Bourse has prevented the formation of a regular stock clearing house in Paris, but the same results are obtained by a voluntary comparison of accounts. The system was not introduced at New York until 1892, when a committee was appointed to investigate and report and their report was promptly adopted. The new plan went into operation on May 16, 1892, and has worked with remarkable success.[1] The necessity of keeping bank deposits to cover the full payment for stock has been brought to an end and accounts are settled by the payment of the balances.

The effect of the withdrawal of so much of the stock exchange business from the New York Clearing House has been marked. Comptroller Knox calculated in 1881 that $113,000,000 of the sum of $141,000,000 received by the State and national banks of New York City on a given day was cleared by twenty-three banks having relations with brokers. An examination of their clearings disclosed the fact that $80,000,000 was in certified checks, of which it was estimated that 90 per cent., or $72,000,000, represented stock transactions. The Comptroller admitted that it was impossible to determine what proportion of these transactions were

[1] Alexander D. Noyes in *Political Science Quarterly*, June, 1893, VIII., 260.

speculative and what proportion for investment, but he computed that about three-sevenths of the whole receipts of the New York banks represented speculative transactions on the Stock Exchange. The falling off in clearings since 1892 has not been nearly so great as this, and the brokers still make large incidental use of the banks, but the establishment of the Stock Exchange Clearing House has introduced a new factor into financial transactions which has to be considered in computing their changes in volume. The record of the operations of three years through the New York Stock Exchange Clearing House is as follows:

NUMBER SHARES CLEARED.	TOTAL VALUE.	REDUCTION OF USE OF CERTIFIED CHECKS.
	From May 14, 1892, to May 1, 1893.	
225,325,800	$15,425,648,200	$4,484,600,000
	From May 1, 1893, to May 1, 1894.	
219,974,200	$13,067,400,000	4,450,880,000
	From May 1, 1894, to May 1, 1895.	
186,192,500	$12,278,700,000	4,363,700,000

II. What has gone before is the best proof of the close relation of the currency to business transactions and that currency should be the hand-maid of commerce rather than the instrument of public power. A government paper currency has rarely been issued to promote the convenience of commerce and has seldom contributed to that end. The success and convenience of paper credit in balancing business transactions has led in many minds to a false analogy between the evidences of such credit and stamped pieces of paper, issued by governments in discharge of public obligations. Governments have even gone further and claimed that the power to issue paper pledges for general circulation, payable to bearer on demand, was an attribute of sovereignty and could not be lawfully assumed by a citizen or a corporation.[1] But this is not the true theory of currency. Experi-

[1] The determination of the legal question is now largely a matter of positive law, but it was admitted in England that at common law the

ence, as well as theory, have proved that government paper money is essentially different in character from banking paper and opens a Pandora's box of evil for every nation which issues it.

The difference between government paper currency and bank-notes is not one of experience or accident merely; it is a difference which is fundamental. Banking institutions are subject to the law; the state is the power which makes the law. Bank paper is based upon business transactions and is limited by their demands; government paper is based upon the will of the state and is limited only by its necessities. The almost invariable rule of government paper issues is that one begets another, until the entire volume exceeds the legitimate demands of business, upsets values, and goes beyond the reach of restoration to the metallic standard. A government is not only not under no restraint of law when tempted to pass the limits of safety in its paper issues, but there are no natural and automatic limits fixed by the conditions of the note issues, as in the case of banks. A banking currency, when not disturbed by the public authority, except to enforce uniformity, safety, and convertibility with coin, is automatically responsive to the demands of business. When business is active such a currency is expansive in proportion to its needs; when business slackens the notes return to their issuers for redemption, the volume of paper money is reduced, and the parity of coin and paper is constantly maintained.

The evils of government interference with the natural

power to issue bank-notes was unrestricted, and in France the power was freely used until after the creation of the Bank of France. The power of the government, according to the soundest modern theories, should be limited to giving an official certificate of the weight and fineness of bullion by fixing a standard coin as the unit; and the failure in the long run to accomplish anything else was illustrated in ancient times by the changes in prices which followed the use of "the power of sovereignty" to debase the value of the coins, and has been illustrated in modern times by the similar changes which have followed the use of the same power to give value to legal-tender paper money.

laws of a banking currency are second only to the evils of direct issues of government paper money. The very solvency and credit which sound banks have attained have been turned against them when they have been seized upon to supply the necessities of governments. This was the case in the infancy of modern banking, when "time and experience," in the language of Cantillon, taught the Venetians that the over-issue of notes for the purposes of war destroyed the parity of coin and paper, upset prices, and diminished the revenue of the republic.[1] It was the case in France, when Necker wrecked the *Caisse d'Escompte* by the advances which he demanded from it. It was the case in England, when Pitt pumped almost dry the reservoirs of the Bank of England to carry on the Napoleonic wars. It was the case in France again, when Napoleon, at the summit of his glory after Austerlitz, returned to Paris to find the Bank of France compromised by advances to the State. It has been more recently the case in Italy, where loans to public men have been governed by political motives rather than the sound rules of commercial transactions. It has been the case also in Spain, where the absorption of the note issues of the Bank of Spain in loans to the government has crippled commerce and flooded the country with a depreciated paper currency. The volume of bank currency in these cases has become no longer responsive to the needs of commerce, but the measure of the hard necessities of the state. Under such circumstances, as M. Clément Juglar remarks of the increase in the Bank of England circulation during the Napoleonic wars, "We are no longer in the presence of a real credit circulation, but of advances which represent no commercial operation; which explains how in more recent times the movements of circulation, released from this pressure, are no longer the same and are obedient to other influences."[2]

The advantage which banks enjoy over the public authorities in controlling the monetary circulation is due to their banking powers. These powers grow out of the connection be-

[1] *Essai sur le Commerce*, 411–12.

[2] *Des Crises Commerciales*, 219.

tween the volume of the currency and commercial movements, but they are exercised by peculiar methods which are beyond the reach of the most skilful and prudent public official. It is the power to push the interest rate up or down which has been proven to be the regulator at once of the foreign exchanges and of the domestic supply of currency and loanable capital.[1] No such automatic regulator can act upon a government paper currency, because the government does not do a banking business. The state is not a money lender nor a receiver of deposits payable on demand. It can neither retain gold at home by raising the discount rate nor govern the volume of its paper issues by business conditions. The Secretary of the Treasury of the United States has sat helplessly in his chair, while the gold reserve has dwindled, armed with no power to arrest the drain unless an enormous surplus permitted the retention of redeemed notes in the Treasury cash. He found himself without this resource in the period of redundant currency which followed the crisis of 1893. The result was an export of gold, under the relentless operation of Gresham's law, which the machinery of the government was powerless to arrest. The mass of needless paper money issued under the Act of 1890 pressed steadily upon the coin and expelled the surplus in the form of gold. What the Treasury proved incompetent to do was accomplished in a measure in the summer of 1895 by a syndicate of banking houses, because of their power to influence the exchanges.

III. While much which has preceded is applicable to the banking powers possessed by banks of discount and deposit, without the power of issuing circulating notes, there remains to be defined a peculiar advantage of banking which cannot be obtained without the power of note issue. This advantage lies in the introduction of banking methods into a country in which they have not attained full development. A banking currency paves the way for deposit banking. It is much easier to found a profitable bank of issue than a

[1] *Vide* p. 17.

bank of deposit, for notes can be quickly put out, based upon capital and the commercial paper offered for discount; but deposits come more slowly by the voluntary act of depositors. Deposit banking is still in its infancy outside Great Britain, Canada, and the United States, as a glance at the relative deposits and note issues of the great Europern banks plainly shows; and even in the United States it has only attained full development in the great commercial cities of the North. The method in which note issues pave the way for deposit banking is well described by Mr. Walter Bagehot thus:

> The way in which the issue of notes by a banker prepares the way for the deposit of money with him is very plain. When a private person begins to possess a great heap of bank-notes, it will soon strike him that he is trusting the banker very much, and that in return he is getting nothing. He runs the risk of loss and robbery just as if he were hoarding coin; he would run no more risk by the failure of the bank if he made a deposit there, and he would be free from the risk of keeping the cash. No doubt it takes time before even this simple reasoning is understood by uneducated minds. So strong is the wish of most people to *see* their money that they for some time continue to hoard bank-notes; for a long period a few do so: but in the end common-sense conquers,—the circulation of bank-notes decreases and the deposit of money with the banker increases. The credit of the banker having been efficiently advertised by the note, and accepted by the public, he lives on the credit so gained years after the note issue itself has ceased to be very important to him. . . .
>
> A system of note issues is therefore the best introduction to a large system of deposit banking. As yet, historically, it is the only introduction; no nation as yet has arrived at a great system of deposit banking without going first through the preliminary stage of note issue; and of such note issues the quickest and most efficient in this way is one made by individuals resident in the district and conversant with it.[1]

In proof of the last assertion may be cited the banking history of Scotland, where the issue of notes is now a trifling part of the liabilities of the banks, but where the profits were originally derived almost entirely from the circulation. The Bank of Dundee, founded in 1763, had for twenty-five years

[1] *Lombard Street*, Works, V., 59–61.

no deposits whatever, but subsisted on the profits of its note issues and some incidental remittance business. Nothing could better illustrate the graphic words of M. Juglar:

> The power of creating bills has this great advantage, that it permits a bank to be born; and this is the important point for small towns, far from great centres, where the channels of circulation of the large banks fail to penetrate. These new promises to pay, added to those of the state, give a new activity to exchanges and place a new capital at the disposition of everyone; and the rate of interest tends to fall and even the intensity of crises is diminished.[1]

A banking currency, therefore, forms the readiest means of introducing the use of credit and stimulating the production of commodities and the transfer of capital. A certain volume of currency of some sort is absolutely essential to the commercial life of a people. The supply varies with commercial habits, and the demand is greatest where the use of credit is least developed and large exchanges are made by the methods of actual barter and cash payment. Bankers, as Prof. MacLeod so happily says, are "dealers in credit." Under a fully developed credit system, the buyer of credits is content to draw checks against the credit transferred to his account, because those checks are readily accepted as a substitute for money. If checks are not readily accepted and if money is lacking, purchases and sales of credit are reduced and capital lies idle and unproductive. Such is the situation of a new country, whose people have neither become generally accustomed to deposit and credit banking nor have the power to issue a credit currency because restrained by prohibitory laws. This poverty of the means of carrying on transactions is a striking feature of the condition of many parts of the Southern and Western sections of the United States, and the remedy lies in an expansive currency which shall make exchange easier and afford the buyer of credit an instrument which he can readily use. The relative equipment of these States in banking

[1] *Des Crises Commerciales*, 183.

power in comparison with the better equipped States of the Northeast is illustrated by the following figures :[1]

STATE.	BANKING POWER PER CAPITA.	STATE.	BANKING POWER PER CAPITA.
Rhode Island,	$377.55	South Dakota,	$21.83
Massachusetts,	328.02	Georgia,	18.53
New York,	298.74	South Carolina,	13.89
Connecticut,	279.35	Mississippi,	10.21
Pennsylvania,	112.81	North Carolina,	9.56
Illinois,	77.98	Alabama,	7.49
Minnesota,	65.38	Arkansas,	6.90

The peculiar advantage of a banking currency issued by a network of local banks is in affording banking accommodation to all parts of the country where the system prevails. In this respect, if in no others, a system of local banks enjoys an advantage over a great national bank in promoting the development of industry and commerce. A government paper currency does practically nothing to promote the banking facilities of the people, and a single bank of issue usually promotes the commerce of the capital where it is located at the expense of the commerce of outlying sections. This was peculiarly the case in France before the establishment of the independent departmental banks and it became the case again after those banks were deprived of the power of note issue. Banking in France was in the primary stage of development, where note issues were essen-

[1] These figures are taken from the Report of the Comptroller of the Currency for 1895, p. 512, and include the aggregate capital, surplus, undivided profits, and individual deposits of national banks on July 11, 1895, and of State, stock savings, and private banks and loan and trust companies at date of latest reports. The average banking power per capita for the United States is computed at $95.83. It is a common opinion, among those who have studied the subject, that this poverty of banking power in the South has greatly stimulated the demand there for a larger metallic circulation, and that laws providing better banking accommodation, by permitting the issue of circulating notes upon general banking assets, would do much to diminish this demand.

tial to profitable banking, and the independent banks made most of their profits by means of note issues and with but trifling private deposits.[1] The promotion of the banking facilities of the capital at the expense of other sections has been the feature of all the great national banks of Europe, —at Vienna and Buda Pesth, at Berlin, at St. Petersburg, and at Madrid,—and the countries in which they are situated have lagged far behind England, Scotland, Switzerland, the United States, and Canada in the development of their industrial activity.[2]

The power to establish branches has not proved a sufficient substitute for the power to create independent banks in the introduction of facilities for credit and in the expansion of commercial operations, where the power of note issue has been lodged in a single great institution. Mandatory legislation was required in France to compel the Bank of France to establish branches in each department and as late as 1865 only fifty-five branches had been created, or at the rate of one for 700,000 inhabitants.[3] The essential defect of branch banking of this sort is the system of bureau-

[1] The aggregate circulation of the nine independent banks in 1847, —the last year before their suppression,—was 90,100,000 francs ($18,000,000), while their deposits on current accounts were only 16,800,000), francs ($3,350,000.)

[2] Mr. Bagehot cites the comparative history of the Bank of France and the banks of Switzerland in proof of the assertion that "A single monopolist issuer, like the Bank of France, works its way with difficulty through a country, and advertises banking very slowly." The note issues of the Bank of France in 1865 were equal to £112,000,000 and the deposits were only £15,000,000. The Swiss banks, on the other hand, showed note issues equal to £761,000 and deposits of £4,709,000. The private deposits of the Bank of France had risen on July 11, 1895, to 426,390,693 francs and private deposits at the branches were 62,873,753 francs, but they amounted together to less than one-seventh of the circulation, which was 3,503,503,270 francs.

[3] Scotland at that time had a branch bank for every 5100 of her people,—the equivalent of 137 times the banking facilities of France. A like multiplication of banking facilities in the latter country would require 10,000 branches of the Bank of France and the number of all classes had risen in 1895 to only 259.

cracy under which it is usually conducted and the absence of sympathy between local business interests and the directing authority at the head.[1] The effect of such a system also in attracting deposits and solvent borrowers is very different from that of a bank managed by men of whom something is known in the locality. The first branches of the Bank of France proved unprofitable, but the independent departmental banks which followed them earned unusual dividends. The reason for the difference is hinted at by M. Horn as follows:[2]

> The countryman, prudent and timid in his nature, confides his small savings willingly only to those whom he personally knows, only to an association sprung from the heart of the local community, only to a bank created and directed by men who have deep root in the locality, only to institutions in which he, his relatives, or his friends are directly interested.

Branch banking may, however, prove of great value in promoting banking facilities if absolute monopoly of note issues does not prevail at the centre of the system. The competition of a few great banks, authorized to issue their own notes through their branches, has proved more successful, in equipping Scotland and Canada with facilities for credit, than the system of smaller local banks, without the power of issuing notes upon assets, has proved in the United States. A system of strong central banks with numerous branches means a much wider extension of banking facilities than would be possible where each bank was independent. It means not only the ready transfer of capital from points where it is plentiful to points where it is lacking, but it means that a community too small to support an independent bank may enjoy the advantage of a branch. A single official, possessing knowledge of local conditions, would preside over a branch and take the place of president, cashier,

[1] Even the slow progress of popular credit banks in France was attributed to the system of centralization which governs her financial policy, by the jury on social economy of the Paris Exposition of 1889. —*Économie Sociale, par Léon Say; Rapport Général*, 322.

[2] *La Liberté des Banques*, 438.

and board of directors of an independent local bank. A small branch would involve no investment in an idle coin reserve, for the funds of the branch would consist in the notes of the parent bank, which would represent no expense until they were issued. The system of branches has resulted in Scotland and Canada in the ready transfer of the savings of the agricultural sections to the manufacturing cities, while the branches in the cities have stood ready to furnish capital for the farming districts on the less frequent occasions when it has been needed. The transfer of capital in this way has been carried on to some extent in England by the practice of rediscounting, but this prevents accurate knowledge of many of the facts regarding the paper offered for rediscount, which would be known to the central bank under the branch system and involves elements of danger readily understood by every banker.[1]

IV. One of the essential conditions of a sound currency is redemption in coin on demand. This is the touchstone and proof of the equality of paper with coin and of the maintenance of the standard of value. A banking currency is usually subject by law to the condition of coin redemption; a government paper currency is rarely subject to such a condition. Governments seldom resort to the issue of paper money until their lack of credit impairs their other resources. Their issues are then expanded to the point where they become redundant, even after they have driven out all other currency and filled its place. An issue too small to become redundant, and which was maintained steadily at par with the metallic standard, would be too small for the purposes which usually control the action of governments in resorting to paper currency.

Even a limited issue of paper is maintained at par by a government with much greater difficulty than by well regulated banks. The reason is fundamental. Governments have no quick assets. The advocates of government paper

[1] "The abuses connected with rediscount by fictitious bills are effectually prevented, and the bank can more readily regulate its advances in accordance with its means."—Gilbart, II., 210.

money are fond of declaring that a national currency is based on the aggregate wealth and credit of the entire nation. But they miss the purpose of currency and of banks of issue. It is not wealth in the abstract which currency must represent, but quickly negotiable wealth.[1] The essential question in regard to government paper money is not whether government and people have wealth, but whether the government is equipped with negotiable assets to do a banking business. Mirabeau missed this distinction, in urging the issue of the *assignats* upon the French Assembly, when he declared:

> They represent real property, the most secure of all possessions,—the land on which we tread. Why is a metallic circulation solid? Because it is based upon subjects of real and durable value, as the land which is directly or indirectly the source of all wealth. Paper money, we are told, will become superabundant; it will drive the metallic out of circulation. Of what paper do you speak? If of a paper without a solid basis, undoubtedly; if of one based on the firm foundation of landed property, never.

It was a plausible argument and if it was a sound one the French paper money should not have depreciated below par, because it did not for a long time exceed in volume the value of the national domains which were pledged as its security. But the *assignats* fell until they were worth one-thousandth part of their face value. The government then put the theory of landed security to a closer test by issuing territorial mandates, redeemable in land on demand, but they fell also to one-fortieth part of their face value and few holders were disposed to take the scattered domains of the state as the equivalent of current money.[2] The distinction be-

[1] "A relative of mine, C. Poulett Thomson, afterwards Lord Sydenham, many years since, used to say to me that nothing was easier to conduct than the business of a banker, if he would only learn the difference between a mortgage and a bill of exchange."—Hankey, 25.

[2] As Blanqui tersely puts it, in comparing the *assignats* with the notes of the Bank of England during the first years of suspension, "The one sort, exchangeable for land, were worth nothing; the others, although deprived of their specie guarantee, preserved their nominal value."—*Histoire d' Économie Politique en Europe*, II., 176.

tween such security and the security of institutions doing a sound banking business, while not always grasped by those unfamiliar with the subject, is of supreme importance. Banking, in the technical sense, consists in dealing in commercial paper for short terms. Few governments have any quick assets beyond the actual coin in their vaults, while a well-managed bank has assets, in the form of commercial paper and securities, in excess of all its liabilities, both to note-holders and depositors, of which all but a small percentage can be quickly turned into cash. The government, beyond its actual cash in hand, has only two corresponding resources—the pledge of public property and the power of taxation. Custom houses and highways, field guns and ironclads, are not the sort of assets which can be quickly marketed or put in pawn to borrow money, and the power of taxation is even less efficient as security for a banking business. It is in the nature of an assessment upon the stockholders, which is a worthless resource during solvency and is resorted to only for liquidation after suspension of payments.[1]

The peculiar strength of a banking currency lies in the enormous mass of quick assets behind its demand liabilities. The United States Treasury, even if all its financial operations of receipt and disbursement are viewed as banking transactions, handles less than one-fifteenth of the average quick assets of the banks of the country and an infinitely smaller proportion of their gross receipts during the year. The largest balance in the Treasury in recent years was $778,604,339 on June 30, 1892. The aggregate capital, surplus, undivided profits, and individual deposits of national and State banks, loan and trust companies, and savings and

[1] "The Treasury is like a bank, in which the stockholders are liable for all its debts, and have bound themselves to put in ample cash capital whenever it is wanted, but in which no cash capital has yet been called up. The Treasury has no bills receivable, no promises of other people to pay its gold coming due from day to day."—Charles C. Jackson, "Why Legal Tender Notes Must Go," *Sound Currency*, Vol. III., No. 2, p. 3.

private banks in the United States, according to reports on or about that date, was $6,390,094,128 and the same items about June 30, 1895, were $6,703,544,084. The capital of the banking institutions of the country, therefore, was not less than eight times the cash assets of the Treasury of the United States and was much less restricted to special objects. For, of government funds on June 30, 1892, $141,325,339 was set aside for the redemption of gold certificates and $326,880,803 for the redemption of silver certificates, leaving only about $310,000,000 to meet all other demands both for daily transactions and for the protection of circulating legal tender notes. A portion of the funds of the banks are set aside for special purposes, but in no such proportion as those of the Treasury.

Turning to the actual flow of money through the Treasury and through the banks, the proportion is still greater in favor of the banks. The gross receipts from all sources of public revenues, including the postal service, during the fiscal year 1895 were $390,373,203, or a little more than $1,000,000 per day. The gross receipts of the banks can only be partially ascertained, but the transactions through the clearing houses alone during the year ending September 30, 1895, were $51,111,591,928, or an average of nearly $140,000,000 per day. In the stream of money pouring through their hands, available to meet current demands, the banks of the United States are, therefore, nearly one hundred and forty times stronger than the Treasury.

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INDEX.

(The names of important banks will be found under the distinctive part of the name rather than under the title "Bank.")

A

Accommodation bills, 468.
Africa, South, banking in, 448–50.
Alabama, experiments with State banking, 332–34.
Algeria, Bank of, 451.
Amsterdam, Bank of, origin, 259; method of redemption, 260; failure, 261; failure to prevent credit crisis, 468.
Arbitrage, contributes to settlement of French war indemnity, 66.
Argentine Republic, banking in, 420–22; speculation before 1890, 519.
Assets, necessity that they be quickly negotiable, 13–15; inefficiency of government assets, 574–75.
Assignats, issue and abandonment in France, 49; Mirabeau's misconception, 573.
Atkinson, Edward, opinion that certificates of deposit are not subject to federal tax, 365, note.
Australia, banking system of, organization, 443; expansion of loans on land, 444–45; clouds in the future, 445–46; withdrawal of British deposits, 522; crisis of 1893, 551–53.
Austria, National Bank of, foundation, 214; effect of specie suspension, 216; attempt to resume, 218; regulations governing circulation, 220; converted into Austrio-Hungarian Bank, 223; loans on securities in 1873, 513.
Austria, struggles with paper money, 209–213; efforts to resume specie payments, 216–18; union with Hungary, 222; adoption of gold standard, 225–27; retirement of paper money, 228; delay in resumption, 229; development of deposit certificates, 234.
Austro-Hungarian Bank, formed from National Bank of Austria, 223; rules governing circulation, 223–24; required to establish gold payments, 227; management of the bank, 231; rate of discount, 232; proposed recharter, 233.
Ayr Bank, based upon landed security, 142; failure, 144.

B

Bank Act of 1844, approved by Sir Robert Peel, 120; purpose of the limit on authorized circulation, 121; operation of the act in 1847, 124; failure to con-

British Linen Company, 142.
Brunswick, Bank of, resists Imperial banking policy, 203.
Bulgaria, National Bank of, 284.
Bullion Report, results from a motion by Mr. Horner, 104; the facts proved, 106; features of the report, 107–9.
Burr, Aaron, secures charter of Manhattan Company, 322.
Business men, failure to grasp theory of currency, 105.

C

Caisse d'Escompte du Commerce, established in France, 46; embarrassed by demands of Calonne and Necker, 48; re-established in 1797, 50; absorbed by Bank of France, 52.
Call loans, not available in a crisis, 14.
Calonne, diverts *Caisse d'Escompte* to public uses, 48.
Cambodia, banking in, 450.
Canadian banking, early history, 387–92; proposals for secured circulation, 393; mania for free banking, 394; issue of Dominion notes, 395; efforts for secured circulation, 396; extension of charters in 1870, 397; advantages of recent legislation, 399; security of note issues, 399–400; elasticity, 401–2; redemption agencies, 403; methods of examination, 404–5; failures, 406–7; reserves, 408; large capital and branches, 409–11.
Canals, development in England, 468; Erie Canal, 480; Suez Canal, 510.
Capital, not increased by note issues, 8–10; regulated by law of supply and demand, 19; accumulation after a crisis, 456; sinking in unproductive enterprises, 461; effect of crises upon distribution, 463–64; withdrawal from United States in 1893, 526.
Carlisle, John G., proposes new banking system, 380–82; proposes changes in national banking act, 383–85.
Cash credits, creation by Royal Bank of Scotland, 162; advantages to Scotch industry, 164.
Central America, banks of, 428–30.
Chamberlain, Hugh, plan for Land Bank, 84.
Chase, Salmon P., conference with New York bankers, 349; interpretation of Act of 1861, 350; issues demand notes, 351–52; relies upon loans, 355; recommends banking system, 357; purpose to pay bank-notes in specie, 361; recommends taxation of state notes, 363.
Cheque Bank, established in London, 128.
Chile, banking in, 416–18.
China, banking in, 441.
Circulation, regulations governing, Italy, 26, 28, 31, 32; France, 58, 61; England, 93, 113, 116, 118, 119, 121, 123; Scotland, 145, 159; Germany, 185, 189, 199–201; Austria, 210, 214, 220, 223, 224, 228; Russia, 245; First Bank of the United States, 289; Second Bank of the United States, 301; Massachusetts, 312–14; New York, 323, 326; Michigan, 328; Louisiana, 337; Wisconsin, 341; under national banking system, 359, 366, 369; Canada, 393, 394, 395, 397, 399–401, 408; Mexico, 415; Chile, 416–18; Brazil, 418; Argentina, 421; Uruguay, 424; Venezuela, 425; Colombia, 426; Ecuador, 426; Haiti, 427; Salvador, 428; Nicaragua, 429; Guatemala, 429; Martinique and Guadeloupe, 430; India, 434, 435; Japan, 437, 439; China, 441; Persia, 442; Australia, 443; South Africa, 448; Cochin-China, 450; Algeria, 451; Senegal, 451.
City of Glasgow Bank, suspension in 1857, 149; failure in 1878, 150; effect upon unlimited liability, 151.
Clay, Henry, denies power of

Congress to create a bank, 293; supports second Bank of the United States, 303–304; resolution to censure Jackson, 306.
Clearing houses, shrinkage of transactions in 1894, 536; transactions in London, 558; transactions in United States, 560–61.
Clearing House certificates, issues in United States, 512; effect of issues in 1884, 518; issues in 1893, 537.
Cleveland, Grover, recommends currency reform, 379; efforts to repeal Sherman law, 534; summons extra session of Congress, 535; opposes silver compromise, 542; recommends retirement of legal tender notes, 545; announces syndicate contract, 546; again recommends retirement of legal tender notes, 549.
Cochin-China, banking system of, 450.
Coin reserve, relation to note issues, 13; the English system, 14; affected by withdrawals of deposits, 15.
Colombia, banking in, 425.
Colonial Bank of London, distribution of circulation, 431.
Compagnie des Indes, develops from the bank of John Law, 42; fall of the stock and readjustment of property, 45–46.
Connecticut, bank-notes affected by depreciated foreign paper, 317.
Consols, origin, 92, note; effect of conversion in 1825, 475–76; conversion in 1888, 518.
Consorzio, established in Italy in 1874, 29.
"Cornering" money, not practicable under free banking, 19.
Costa Rica, banking system, 430.
Cotton, subject of Biddle's speculations 484; new markets opened in 1861, 501.
Council bills, sale by Indian government in London, 436.
Crawford, William H., supports Bank of the United States, 293.
Credit, gives monetary value to gold as well as paper, 3; use of checks, 10; seems to multiply capital, 10; effect on crises, 454–55; relation to note issues, 465; economy in use of coin, 556; proportion in receipts of Bank of France, 560; proportion in transactions in United States, 561; promoted by a banking currency, 568.
Crimean war, effect on commerce, 495, 498.
Crises, not caused by bank-note issues, 12; distinctive classes, 435; origin and development, 454; effect on merchandise markets, 456; effect upon bank accounts, 457–58; advantages of liberal accommodation, 459–60; sinking of capital, 461–62; effect upon distribution of wealth, 463; influence of bank notes, 465; early history, 467; crisis of 1783, 469–70; of 1810, 470–72; of 1814–19, 472–75; of 1825, 475–79; of 1837–39, 479–87; of 1847, 487–91; of 1857, 492–99; of 1864–66, 499–508; of 1873–79, 509–14; of 1882–84, 514–18; of 1890, 518–23; of 1893, 524–54.
Cuba, Spanish Bank of, 431.
Currency principle, distinguished from banking principle, 7; adopted by Sir Robert Peel, 120; ignores use of credit, 122; failure in the crisis of 1844, 124; connection with convertibility of notes, 127; advocated in Canada, 392–93.

D

Dallas, Alexander J., plan for a national bank, 294.
Darien Company, competition with Bank of Scotland, 139.
Delaware, banking in, 337.
Demand notes, issued by Secretary Chase, 351; cause specie suspension, 352.
Departmental banks in France, foundation, 53; suspension of specie payments, 57; fusion

with Bank of France, 58; operate without deposits, 570.
Deposits, how affected by crises, 458.
Discount rate, folly of attempting to maintain a uniform rate, 18; method of Bank of France, 71; system of rapid changes adopted by Bank of England, 129; changes in leading banks, 136.
Dominion notes in Canada, issue authorized, 395; required in bank reserves, 397; may be demanded at banks, 401.
Dutch East India Company, borrows from Bank of Amsterdam, 261.

E

Eckels, James H., modifies system of bank examinations, 375; recommends new basis for banks of issue, 385.
Ecuador, banks of, 426.
Elasticity, fluctuations with the seasons in Scotland, 156; essential benefit of a banking currency, 566.
England, Bank of, exchanges gold for silver with Bank of France, 67; conditions of creation, 78–81; Paterson's plan, 81; political dangers, 84; financial dangers, 86–90; monopoly of note issues, 93; suspension of specie payments. 95–98; effect of specie suspension, 101; bullion report, 106–9; resolutions of Mr. Vansittart, 110; resumption of cash payments, 114; monopoly of note issues modified, 116; adoption of currency principle, 120; failure of currency principle, 124; changes in discount rate, 129: the "one reserve system," 131; organization, 134; increase of discounts in 1810, 471; policy in the crisis of 1825, 477; issue of £1 notes, 478; supported by the Barings in 1839, 486; suspension of Bank Act in 1847, 490; suspension of Bank Act in 1857, 497; suspension of Bank Act in 1866, 505–7; distrust of bank abroad, 508; well equipped in 1875, 514; management in crisis of 1890, 520–21.
England, economic position in 1697, 87; extension of international banking, 414, note; legislation against stock jobbing, 467; accommodation bills, 468; contraband trade with Germany, 471; speculation after fall of Napoleon, 473; scarcity of cereals in 1818, 474; speculation in 1825, 476; railway extension, 488; absorption of capital in 1857, 493; joint stock companies in 1864, 502; distrust of British credit abroad, 508; crisis of 1875, 514; loans in Argentine Republic, 518.
Equivalent fund, made the basis of Royal Bank of Scotland, 141.
Examination of banks, method under national banking law, 375; method in Canada, 404.
Exchequer bills, effect of issue in 1793, 470; issue of 1811, 472.

F

Finlands Bank, 249.
Florida, State banking, 335–36.
Foreign exchanges, influence on redundancy of the currency, 16; method of controlling, 17; method of management by Bank of France, 71; employed to maintain gold standard in Java, 447; effort to control by syndicate contract, 547; defects of system, 548.
France, invaded by Italian subsidiary coin, 34; origin of banking, 38; the Mississippi Company and the plans of John Law, 39–45; collapse of Law's system, 45; banking before the Revolution, 46–49; issue of the *assignats*, 49; the *Caisse des Comptes Courants* and *Caisse d'Escompte*, 50; foundation of the Bank of France, 51; the independent departmental banks, 53–57; effects of the

double standard, 66; character of the Latin Union, 67–70; position of the Bank of France, 75–77; collapse of credit in 1805, 470; effects of Napoleon's fall, 472; abuse of credit in 1837, 486; condition in 1847, 491; benefits of gold discoveries, 500; craze for stock companies, 503; speculation in securities, 515.

France, Bank of, foundation, 51; reorganization by Napoleon, 52; resistance to monopoly of the bank, 56; suspension of specie payments, 57; assists railway enterprises, 59; influenced by the war with Germany, 60; threatened by the Commune, 61; assists in paying war indemnity, 62–65; embarrassed by variations between gold and silver, 66; changes in limit of circulation, 72; gold and silver holdings, 73; government of the bank, 76; proposed renewal of charter, 77; dangerous position in 1805, 470; expansion of discounts in 1810, 471; fall of metallic reserve in 1818, 475; strong position in 1825, 479; loans to Bank of England in 1839, 486; purchases of gold in 1847, 491; losses of gold in 1857, 498; character of receipts, 560.

Franco-Prussian war, effect on Bank of France, 60–65; effect on National Bank of Belgium, 253–55; cost, 509; effect on Germany, 510; effect on Bank of England, 513; effect on France, 515.

Free banking, outlines of the theory, 2; prevents the cornering of currency, 19; does not imply absence of uniform regulations, 20; illustrated by Swiss system, 270.

Free banking law in New York, its features, 326; issues by individuals, 327; similar laws adopted in Western States, 329; failure in Wisconsin, 341.

French Revolution, effect on banking in Italy, 25; on credit in France, 49; upon Bank of England, 95–98.

G

Gallatin, Albert, supports Bank of the United States, 292; opinion of specie suspension, 293.

Geneva, Bank of, 268.

Genoa, Bank of, origin and political power, 22–23; the later bank of 1844, 25; unites with National Bank of Sardinia, 26–27.

Germany, terms of the French war indemnity, 62–65; banks of Prussia, 182–86; banks of the German States, 186–89; limiting circulation of foreign bills, 189–91; centralizing policy of Prussia, 191–92; adoption of gold standard, 193–94, Bank of Hamburg, 195; unification of banking system, 196–97; the Imperial Bank, 198–201; regulation of local banks, 201–5; popular loans of the Imperial Bank, 207; cost of war with France, 509; effects of war indemnity, 510; speculation in 1873, 513.

Godfrey, Michael, share in organizing Bank of England, 81, describes business of the bank, 83.

Gold, derives value from character as money, 3; variation from coinage ratio in France, 66; relation to paper in England, 102; relation to prices, 106; favored as the standard by German cities, 193; adopted as the standard in Germany, 194; recommended as standard in Austria, 225; importations into Austria, 228; accumulation in Russia, 245; certificates in Russia, 248; maintenance of the standard in Holland, 263; method of maintaining the standard in Java, 447; withdrawals from England in 1818,

474; new coinage policy in United States, 482; effect of opening American mines, 493; disappearance in France, 1857, 498; benefits of new supplies in France, 500; borrowed by Bank of England abroad in 1890, 521.
Goschen, Sir George J., adopts rule of rapidly raising discount rate, 129–30; proposes £1 notes, 131–32.
Great Britain, *see* England, Scotland, and Ireland
Greece, banking in, early history, 277; relations with the government, 278; economic condition of country, 278–79.
Guadeloupe, Bank of, 430.
Guaranteed Banking Act in Argentina, 421; results in speculation, 519.
Guatemala, banking laws, 429.
Guiana, banks of, 430–31.

H

Haiti, banking system of, 427.
Hamburg, Bank of, history and liquidation, 195; failure to prevent crisis of 1763, 468; failure to prevent crisis of 1857, 499.
Hamilton, Alexander, deceived in regard to landed security, 34; plan for Bank of the United States, 288; change of views regarding landed security, 289, note.
Holland, banking in, Bank of Amsterdam, 259–61; Bank of the Netherlands, 262–63.
Hongkong and Shanghai Banking Corporation, 441.
Horner, Francis, moves for an inquiry regarding currency and exchanges in England, 104; prepares Bullion Report, 105; resolutions defeated in Parliament, 110.
Houblon, Sir John, first Governor Bank of England, 82; stays a panic, 86.
Hungary, demands payments from National Bank of Austria, 222; relations with Austro-Hungarian Bank, 223; adoption of gold standard, 225; Separatist feeling affects bank charter, 233.

I

Illinois, failure of State banks, 336–37.
Imperial Bank of Germany, created from Royal Bank of Prussia, 196; organization, 197; rules governing circulation, 199–201; rate of discount, 201; gold holdings, 206; relations with popular banks, 207.
Imperial Ottoman Bank, organization, 281; effects of panic on circulation, 282.
Independent Treasury system, outgrowth of conflict over Bank of the United States, 308; modified in 1861, 349; fails to prevent specie suspension, 353.
Indemnity of France to Germany, share of Bank of France in its payment, 62–64; effect on securities, 65–66.
India, early banking history, 433; adoption of government paper currency, 435; effect of suspending free coinage, 436; report of Currency committee, 533.
Indiana, success of State Bank, 338; the new bank, 339.
Interest, opposed among Christians, 23; paid on notes of suspended banks in Scotland, 140; allowance on deposits benefits Scotch people, 159–62; paid on notes of suspended banks in Canada, 400.
Ireland, depreciation of currency considered by Parliamentary committee, 103; economic fortunes, 167; savings of the people, 181.
Ireland, Bank of, foundation, 171; monopoly of banking, 173; circulation, 180.
Ireland, banking in, early private banks, 168–70; foundation of Bank of Ireland, 171; suspen-

sion of cash payments, 172; the Provincial Bank, 174; National Bank, 175; Tipperary Bank, 177; Banking Act of 1845, 178-80.
Italy, early banking history, 29-35; National Bank of the Kingdom, 27; policy of unity in banking, 28; corruption among officials, 30; flight of subsidiary money, 34; present economic condition, 35; popular banking, 36-37; participates in Latin Union, 68; facts crisis of 1893, 525.
Italy, National Bank of, created by Victor Emanuel, 27; loans to government, 29; illegal circulation, 30; absorbs National Bank of Tuscany and Tuscan Bank of Credit, 31; new organization in 1893, 32; relations with the Roman Bank, 35.

J

Jackson, Andrew, criticises Bank of the United States, 302; determines to suspend deposits in bank, 305; protests against Senate resolutions, 306; issues specie circular, 481.
James I., policy of raising taxes, 82.
Japan, early banking history, 437-38; the Bank of Japan, 439; effect of silver standard, 440.
Java, Bank of, organization, 446; method of maintaining gold standard, 447.
Jay Cooke & Co., failure of, 511.
Jefferson, Thomas, policy towards Bank of the United States, 291.
Joint stock banks, discovered to be legal in England, 115; first bank established in London, 117; lack of coin reserve, 130.
Joint stock companies, effect on production, 402, note; variety of objects in England in 1825, 490; expansion in England in 1824, 483; effect of Limited Companies' Act, 502; expansion in France, 503; absorption of capital in Prussia, 510; speculation in Vienna, 513; development in France up to 1882, 515; expansion in England up to 1890, 518.

K

Kentucky, banking in, 330-31; relief laws, 332.
King, Lord, issues a circular to tenants requiring payments in coin, 111.

L

Labor, employed from past savings, 455; affected by crises, 463.
Land Bank, projected by Chamberlain, 84; collapses, 85.
Land, not a proper security for bank-notes, 15; fails in England, 87; leads to collapse of Ayr Bank, 143; causes failure in Ireland, 168-169; failure as security in Belgium, 252; failure in Paraguay, 423; evil results in Australia, 444-45, 552; failure in France, 573.
Latin America, banks of, 412-13.
Latin Union, conference of 1893 regarding redemption of Italian subsidiary coins, 34; originated in a proposition from Belgium, 67, 255; attempts to maintain circulation of silver, 68; makes gold primary money, 68; limitation of silver coinage, 70; effect of the Union upon Bank of France, 71; exchange of minor coins, 256.
Law, John, foundation of the *Compagnie d' Occident*, 39; contracts with French government, 41; continued issue of stock, 42; collapse of the system, and attack upon Law, 45.
Legal tender, in Italy, 26, 27, 32; in France, 44, 57, 60; in England, 98, 118; in the German States, 189; in German Empire, 206; in Austria, 216, 221; in United States, 353; in New South Wales, 445; in Algeria, 451.

Legal Tender Notes, President Cleveland recommends retirement, 545, 549.
Lidderdale, William, skilful management of Bank of England in 1890, 520.
Limited liability, its adoption in Great Britain in 1858, 151; modified in 1879, 152.
London clearing house transactions, 558.
Louisiana, banking system, 337.

M

Machinery, influence on overproduction, 462–63.
Macleod, Prof. Henry Dunning, demonstration that value is not an inherent quality, 3; theory of credit and banking, 8–9; theory of discounting, 17.
Madison, James, suggests a national bank, 295; change of constitutional views, 296.
Maine, banking laws, 315; specie in banks in 1861, 340.
Marshall, John, decision regarding national bank, 296.
Martinique, Bank of, 430.
Massachusetts, Land and Manufacturing Bank, 286; early banking laws, 312; banks maintain specie payments, 313; increase in banks prior to panic of 1837, 314; Suffolk banking system, 317–21.
McCulloch *vs.* Maryland, decided by Marshall, 296.
McCulloch, Hugh, appointed Comptroller of the Currency, 361; recommends taxation of State bank-notes, 363; recommends resumption, 367.
Melbourne, Bank of, 446.
Mexico, banks of, 414–16.
Michigan, wildcat banking in, 328–29.
Mississippi, failure of State banks, 334–35.
Mississippi Company, *see Compagnie des Indes.*
Missouri, banks of, 337–38.
Monetary conferences, international, in 1878, 531; in 1881, 531; in 1892, 532.
Montreal, Bank of, foundation, 387; issues provincial notes, 395; favors secured circulation, 396.
Morgan, J. Pierpont, syndicate contract with Treasury, 546–48; subscription to loan of 1896, 550.
Morris, Robert, founds Bank of North America, 287.
Mortgages as security, *see* Land.

N

Nassau Bank, 431.
National banking system of the United States, comparison with State systems, 344–46; originates in difficulties of the Treasury, 349–57; Secretary Chase's plans, 358; rules governing circulation, 360; objections met by Comptroller McCulloch, 362; taxation of State notes, 363–64; changes in circulation, 365–67; resumption of specie payments, 367–69; extension of charters, 371; effect of Bland Act and Sherman Act, 373; redemptions, 374; examinations, 375; efforts for a new system, 377–85; failures in 1893, 530, 535; expansion of banking capital, 539; effect of the reserve system, 539–40; changes in discounts and deposits, 543.
Necker, exacts secret loans from *Caisse d'Escompte*, 48.
Netherlands, Bank of, succeeds Bank of Amsterdam, 261; method of maintaining the gold standard, 263.
New Brunswick, banking in, early charters, 391; brought under Canadian law, 396; branches, 410.
New England banks, illustrated by Massachusetts system, 312; legislation in Maine and Vermont, 312; in Rhode Island, 316; Suffolk system, 317–21; suspension of 1861, 321; effect on circulation and specie re-

O

P

R

Redemption of bank-notes, method under national banking system, 374–75; changes recommended by Secretary Carlisle, 384.
Redemption of United States notes, 545, 549.
Relief laws, in Kentucky, 332.
Restriction of cash payments in England, 98; effect upon bank-notes, 101–4; brought to an end, 114.
Resumption, recommended by Secretary McCulloch, 367; supported by national banks, 368.
Réunion, Bank of, 452.
Rhode Island, law for recovery of bank debts, 316; agency of Suffolk redemption system, 318.
Roman Bank, foundation, 28; exceeds legal circulation, 30; compelled to liquidate, 31, 35.
Roumania, banking in, 283–84.
Royal Bank of Scotland, created from the Equivalent Fund, 141; establishes branch in London, 154; establishes cash credits, 162.
Russia, Bank of, close relations with the state, 235; origin and capital, 238; plans for specie resumption, 240; revision of charter, 241; rules governing circulation, 244–45; steps towards gold payments, 246–48.
Russia, paper money issues, 236; efforts to restore specie payments, 237–40; new industrial policy, 243; steps towards gold standard, 246–48; loan to Bank of France in 1847, 491; exchange of silver with Bank of France in 1861, 501; loans to Bank of England in 1890, 521.
Russo-Chinese Bank, 442.

S

Safety fund system, adoption in New York, 323; failure and its causes, 324–25.
Salvador, banks of, 428.
Sardinia, National Bank of, created in 1849, 26; reorganizes as National Bank of Italy, 27.
Scotch banking system, its early history, 138–43; strength during specie suspension, 145; failure of the Western and City of Glasgow Banks, 146–50; limited liability, 150–52; proposal to abolish Scotch note issues, 153; advantages of Scotch banking, 155–66.
Scotland, Bank of, foundation, 139; increase of capital, 144; application for limited liability, 152; establishes branch in London, 154.
Scotland, origin of accommodation bills, 468; failure of Western Bank, 497; failure of City of Glasgow Bank, 514.
Securities, introduced in France by John Law, 41; effect of French indemnity loan upon price, 65–66; tendency to return to country of origin, 229; effect of official sales in France, 475; new method of financing, 502; extension in France, 515; effect on trade statistics, 516; American, held in Europe, 526; shrinkage in dividends in 1895, 529.
Senegal, Bank of, 451.
Servia, National Bank of, 284–85.
Sherman law, effect on bank circulation, 373; efforts of President Cleveland to repeal, 524; effect on gold exports and Treasury reserve, 527; repealing bill, 540; action in House, 541; repeal, 542.
Sicily, Bank of, foundation, 28; exceeds legal circulation, 30; subject to law of 1893, 33; assists people's banks, 37.
Silver, fluctuations embarrass Bank of France, 66; causes the formation of Latin Union, 68; change in the commercial ratio, 69; limitation of coinage, 70; effect upon circulation of Bank of France, 72; disappears from England, 101; principal metallic stock of Germany, 192; standard of the Bank of Ham-

U

Ultramarine Bank, 452.
Union Générale, failure of, 517.
United States, suspension of specie payments in 1814, 474; crisis of 1837, 479–83; exports of 1847, 487; railway extension in 1857, 493; changes in circulation, 495; crisis of 1857, 496; effect of civil war, 500; crisis of 1873, 511–12; crisis of 1884, 517; crisis of 1893, 524–50; transactions of clearing houses, 560; proportion of credit instruments, 561; advantage of banks over the Treasury, 574–75.
United States, Bank of, origin, 287; relations with Treasury, 289–91; expiration of charter, 292; plans for second bank, 294–95; constitutional opposition to the new bank, 296; case of McCulloch *vs.* Maryland, 297; specie resumption, 298; branch drafts, 301; arouses hostility of Jackson, 302–4; removal of the deposits, 306; origin of sub-Treasury system, 307–9.
United States, banking in, *see* United States, Bank of, State banks, and national banking system.
Uruguay, banking in, 423–25.

V

Van Buren, Martin, recommends safety fund system, 322; calls extra session of Congress, 483.
Vansittart, opposes bullion report, 110.
Venezuela, banking law, 425.
Venice, Bank of, transfer office of the national debt, 21; deposit bank created, 22.
Vermont, banking in, 315; encourages Suffolk system, 320.
Victoria, banking laws of, 443; estimated wealth in 1892, 551.
Vienna, Bank of, creation and failure, 210.
Vienna, speculation in 1873, 513.

W

Webster, Daniel, favors creation of a commercial bank, 294; secures amendment of bank bill, 296; opinion in favor of branch drafts, 301.
Western Bank of Scotland, adopts policy hostile to that of other Scotch banks, 147; failure and heavy losses, 148–49; effect of failure, 497.
West Indies, British, banks of, 430–31.
Wilson, William L., bill to repeal Sherman Law, 540; bill to authorize gold bonds, 546.
Wisconsin, failed banks, 330; decline in southern securities, 340–41.
Witte, Russian finance minister, new organization of Bank of Russia, 241–44.

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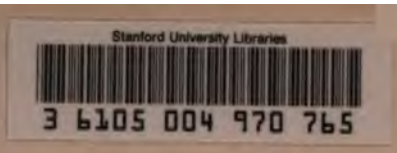

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